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Cause Nos. 17-0640 and 17-1048

IN THE SUPREME COURT OF TEXAS

Barbara Technologies Corp., *Petitioner*

v.

State Farm Lloyds, *Respondent*

Oscar Ortiz, *Petitioner*

v.

State Farm Lloyds, *Respondent*

Brief of *Amicus Curiae* Texans for Lawsuit Reform

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Statement of Interest

Texans for Lawsuit Reform (TLR) is a volunteer-led non-profit organization founded in 1994 to help foster and maintain a system that achieves a fair, merits-based resolution of civil disputes in a quick and efficient manner, so as to encourage economic development and job creation in Texas. Thousands of individuals—living in towns and cities across Texas and representing virtually all of Texas's trades, businesses and professions—support TLR's mission.

TLR has no direct or indirect financial interest in this matter. TLR has an interest in the public policy issues presented by these cases. In 2014, we began to hear that the number of lawsuits filed against private-market insurers following weather-related events was increasing precipitously. Our study of the legal landscape confirmed a marked increase in these lawsuits, driven in large part by an expansive view of Texas's Prompt Payment of Claims Act (TPPCA). *See*, *generally*, TEX. INS. CODE Ch. 542, Subch. B. Consequently, we supported legislative efforts during the 84th (2015) regular session of the Texas Legislature to address the problem, but these efforts failed.[1]

[1] TLR supported passage of Senate Bill 1628 and House Bill 3646, which were companions.

During the interim between the 84th and 85th legislative sessions, TLR conducted an in-depth study of the weather-related litigation issue. This research further confirmed an unusual spike in lawsuits against private-market insurers.[2] Based on the data TLR accumulated from clerks' offices across Texas, for the six-year period from 2006 to 2011, an average of 744 property and casualty insurance lawsuits had been filed statewide against private-market insurers.[3] In 2012, however, almost 2,000 such lawsuits were filed. In 2013, the number of these lawsuits more than double 2012's filings. In 2014, over 10,000 of these lawsuits were filed; and just under 10,000 more were filed 2015.[4]

TLR was not alone in concluding that the number of private-insurer lawsuits had exploded. The Texas Department of Insurance (TDI) provided a

[2] TLR does not take the position that all increases in lawsuit filings indicate a problem requiring a legislative solution. In some instances, an increase in lawsuit filings may be justified by events or changes in law.

[3] TLR gathered data from about 175 of Texas's 254 counties, and that number changed over time. For example, Maverick County, which experienced a significant increase in insurance lawsuit filings in the mid-2000s, stopped reporting data in 2016. Additionally, our method for identifying qualifying lawsuits often required the exercise of judgment. Consequently, the data we are providing should be regarded as showing only the magnitude of the problem. TLR's data probably under undercounts the number of qualifying lawsuits filed in Texas.

[4] Webb County, Texas, is an example of the weather-related lawsuit explosion seen in the mid-2000s. Webb County (Laredo) averaged sixteen insurance lawsuit filings per year from 2006 through 2013. In 2014, the number of new insurance lawsuits jumped to 704. In 2015, the number of insurance lawsuits spiked at 1,912—about 120 times the historic average. The problem was not limited to any geographic area of the state. Potter County (Amarillo) saw its average increase from about seven insurance lawsuits per year to 781 such lawsuits in 2015—a 110-fold increase. In a typical year in Bell County (Killeen/Temple), a single insurance lawsuit *might* be filed (in many years, none were filed). But in 2014, 155 such lawsuits were filed and in 2015 another 154 were filed.

report to the Texas Legislature in February 2017, concluding that property and casualty insurance litigation in Texas had increased 1,400 percent since 2011.[5] TDI also found that the lawsuit explosion was affecting both competition and cost, with seven insurance companies withdrawing from some counties and a dozen companies reporting an increase in rates charged to consumers as a direct result of the litigation environment in Texas.

We determined that a driving force behind the litigation spike was the quest to recover attorney fees, particularly under the TPPCA, which was being interpreted by some attorneys and trial courts to allow the recovery of fees if an insurance claim was underpaid by a single dollar.

To address this lawyer-driven increase in weather-related litigation in Texas, the Texas Legislature passed House Bill 1774 during its 85th (2017) regular session.[6] Governor Abbott signed the bill into law. TLR advocated vigorously for passage of H.B. 1774, providing our research to Texas policymakers.

H.B. 1774 added Chapter 542A to the Texas Insurance Code. It applies only to insurance claims arising from a loss caused by "forces of nature, including an earthquake or earth tremor, a wildfire, a flood, a tornado, lightning,

[5] *See* https://www.tdi.texas.gov/reports/documents/weatherrelatedpropertyclaims.pdf.

[6] *See* Tex. H.B. 1774, 85th Leg., R.S. (2017).

a hurricane, hail, wind, a snowstorm, or a rainstorm." TEX. INS. CODE § 542A.001(2). The heart of Chapter 542A is to strengthen the existing requirement[7] that an insured provide notice to an insurer before filing a weather-related lawsuit against the insurer. *See id*. § 542A.003. The new notice provision is enforced by an abatement of the lawsuit *and* the possibility of a diminished fee recovery by the insured's attorney. *See id*. §§ 542A.005, 542A.007(d).

Chapter 542A also addresses the problem of overclaiming by insureds' attorneys. Asserting damages far beyond an amount anyone would consider reasonable—overclaiming—was common in the thousands of weather-related lawsuits filed in the mid-2000s. The theory of overclaiming is that if the insured's lawyer can persuade the finder of facts that any element of the claim was unpaid or underpaid, then the attorney is entitled to recover all attorney fees billed to the file. It is thought that the larger the claim in both scope and value, the more likely it is that the finder of facts will conclude that some element of the claim was unpaid or underpaid. This quest to recover attorney fees drove weather-related litigation. Chapter 542A addresses overclaiming by

[7] A pre-suit notice requirement already existed in both the Insurance Code and the Deceptive Trade Practices Act, but the enforcement mechanism (temporary abatement) meant that it was routinely ignored during the bulk-filing of insurance lawsuits in the mid-2000s. *See* TEX. INS. CODE §§ 541.154, 541.155; TEX. BUS. & COMM. CODE § 17.505(a), (c)-(e).

requiring trial courts to compare the amount demanded in the pre-suit notice to the putative judgment, and then reduce the fee recovery if the pre-suit demand significantly exceeds the amount to be awarded to the insured in the judgment. *See id*. §§ 542A.005, 542A.007(a)-(c).

TLR's concern is that this Court's interpretation of the TPPCA in these cases suggests that the TPPCA allows recovery of the full measure of attorney fees if a claim is unpaid or underpaid by a single dollar, even when there is a legitimate dispute about coverage or the amount owed on a covered claim. We fear a return to 2015, not just in weather-related insurance cases, but in relation to any insurance claim governed by the TPPCA. Thus, TLR's interest in this case is to advocate for what we believe is the proper and logical reading of the TPPCA, so as to avoid unnecessary litigation, the cost of which is passed through to consumers in the form of higher premiums and deductibles and reduced competition in the insurance market.

TLR has paid all fees incurred in preparing and filing this brief.

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Brief of *Amicus Curiae* Texans for Lawsuit Reform

TO THE HONORABLE SUPREME COURT OF TEXAS:

In the context of these cases, the meaning of Texas's Prompt Payment of Claims Act (TPPCA or Act) revolves around three words: "pay the claim." We do not think these words require an insurer to pay all amounts ultimately found to be owed through a dispute-resolution process. Instead, we believe these words mean an insurer must pay the amount it acknowledges is owed, if any, within the statutory deadline. If it pays the amount it acknowledges is owed and timely

performs the other steps required by the Act, there is no liability *under the TPPCA*, no matter what subsequently happens. If the parties find themselves in a disagreement about the amount owed under the insurance contract, they may proceed through the appraisal process or litigation. These dispute-resolution methods may or may not result in a payment by the insurer to the policyholder, but either way, the TPPCA is not implicated so long as the insurer met all of the Act's deadlines and paid the amount it determined to be owed on the claim.

Our interpretation of the TPPCA is consistent with the words used by the Legislature and with the rules of statutory construction, it conforms the Act to the overall statutory scheme, and it leaves the appraisal process undisturbed. We are concerned that the Court's current interpretation of the Act, on the other hand, will cripple the contractual appraisal process and invite the mass filing of lawsuits. Consequently, Texans for Lawsuit Reform, as *amicus curiae*, files this brief to urge the Court to grant the Respondent's motion for rehearing and reconsider its interpretation of this important statute.

A. Introduction

In the simplest terms, the TPPCA requires insurers to quickly acknowledge receipt of a policyholder's claim, quickly begin to investigate the claim, quickly decide how much the insurer is willing to pay on the claim, immediately pay the amount the insurer has decided is owed, and explain its

refusal to pay any part of the claim. If an insurer follows these steps, the Act's terms are fulfilled and the Act's goals have been accomplished—prompt consideration and payment of the claim, if any payment is going to be made. If an insurer does not promptly process, evaluate, and pay whatever amount the insurer is willing to pay, the insurer has liability under the Act. In short, the Act is designed to prevent insurers from sitting on claims that are going to be paid.

If a policyholder believes the insurer has wrongfully refused to pay for all or part of a claim, the policyholder may pursue a breach of contract action against the insurer to recover the amount owed, pre- and post-judgment interest, and attorney fees. If a policyholder believes the insurer conducted a bogus investigation, refused to pay a claim when its liability was clear, or otherwise handled the claim in an unfair manner, the policyholder may pursue an action against the insurer under the Unfair Claim-Settlement Practices Act (UCSPA) to recover actual damages, treble damages, pre- and post-judgment interest, and attorney fees. *But the failure to pay part or all of a claim that is later determined to be owed through litigation, appraisal, or otherwise—in our reading of the Act—does not give rise to damages under the TPPCA.*

The contractual appraisal process, which is the subject of the present cases, can and does co-exist with the TPPCA. Again, if an insurer has followed the statutorily mandated steps (which includes the prompt payment of

whatever amounts the insurer agrees is payable), the Act is satisfied and no longer provides a cause of action. The fact that the appraisal process may result in an additional payment to the policyholder is of no relevance to the TPPCA. Neither is it relevant that the insurer is later adjudged to owe additional amounts on the claim. These subsequent events cannot change what an insurer was required to do at the time of the Act's deadline. Otherwise, insurers will be statutorily required to accurately predict that a dispute over the claim payment will occur *and* accurately predict the ultimate resolution of that dispute before a third-party arbiter. As unsympathetic as insurance companies may be, this is not a fair burden to place on insurers (or any business).

Our interpretation is fully supported by the words of the Act and by rules of statutory construction. It prevents the evisceration of the appraisal process, which can be used to achieve the prompt, fair, and inexpensive resolution of claims. It also avoids creating an unnecessary liability scheme that punishes a party who is engaged in a legitimate dispute about the value of an insured loss. All the while, other statutory remedies remain to address insurers who engage in bad conduct and wrongful denials.

B. The Prompt Payment of Claims Act has a definite meaning.

The Prompt Payment of Claims Act is far from the hallmark for statutory clarity, but it has a definite and ascertainable meaning. It is full of instances

when helpful words and phrases are simply omitted. Section 542.055(a), for example, allows an insurer to request from the claimant "all items, statements, and forms that the insurer reasonably believes, at that time, will be required from the claimant." TEX. INS. CODE § 542.055(a)(3). One might ask: "Items, statements, and forms *required* to do what?" A reasonable interpretation is that the insurer is being permitted to request the items, statements, and forms needed to evaluate the claimant's request for payment under the insurance policy, but the Act does not actually say that.

The next sentence in the Act tells us that the insurer can "make additional requests for information if during the investigation of the claim the additional requests are necessary."[8] *Id.* § 542.055(b). Again, a person might ask: "Necessary to do what?" The sentence does not say that the request for information must be sent to the claimant and does not require that it be necessary for a particular purpose. Read literally, an insurer could request anything from any person, so long as it deems the information "necessary." Of course, such an interpretation of the Act would be counter-intuitive and inconsistent with the Act's purpose. A reasonable interpretation of the Act is that it allows the insurance company to gather the documents and information

[8] Is "information" different than "items, statements, and forms" or did the Legislature intend for "information" to be shorthand for "items, statements, and forms"?

it needs to evaluate the policyholder's request for payment under the contract. But the Act does not actually say that.

Section 542.056 requires acceptance or rejection of the claim within fifteen days after the insurer receives all items, statements, and forms "required by the insurer to secure final proof of loss." *Id.* § 542.056(a). What does it mean to "secure final proof of loss"? Again, we must infer the Legislature's meaning, because no definition is provided. A reasonable construction is that it means the insurer must accept or reject the claim within fifteen days of receiving all documents and information it needs to determine whether the loss is covered by the policy and, if so, the amount required by the policy to be paid for the covered loss. But thats just an inference based on common sense and context clues. It is not based on the literal text, read in a vacuum.

Section 542.057 provides that "if an insurer notifies a claimant *under Section 542.056* that the insurer will *pay a claim* or *part of a claim*, the insurer shall *pay the claim* not later than the fifth business day after the date notice is made." *Id*. § 542.057(a) (emphasis added). The problem here is that section 542.056 does not require an insurer to notify the claimant whether it will "pay the claim." Instead, section 542.056 requires a notice as to whether the insurer is accepting or rejecting a claim. Here, it appears the Legislature is equating

acceptance and payment, while also equating rejection and nonpayment.[9] But, again, the meaning must be derived from the context, not from the literal words.

The point here, of course, is that while the TPPCA is not the model of clarity, its meaning is ascertainable from the words used by the Legislature.

C. When does an insurer have liability under the Act?

The Prompt Payment of Claims Act describes two circumstances in which insurers must pay statutory interest (deemed "damages" by section 542.060(a)) and attorney fees:

First: If an insurer "delays payment of the claim for a period exceeding the period specified by other applicable statutes or … for more than 60 days" after it receives all reasonably required items, statements, and forms requested under section 542.055, it must pay interest and attorney fees "as provided by Section 542.060." TEX. INS. CODE § 542.058(a). And so, the standard for liability under section 542.058 is a "delay in payment of the claim." It follows, then, that if the insurer timely pays the claim—whatever "pay the claim" means—it does *not* have liability under the Act.

[9] We would not dispute an assertion that the statute is oversimplified and inexact. There is no specific accounting in the language of the Act, for example, for a claim that may fall within coverage, but the amount owed on the claim is within the policy's deductible. In reality, the deductible could be satisfied in part, but no money is owed; and then if a second claim is received and accepted, it too would impact the deductible and might result in a payment on the claim. Oversimplified or not, the statute says what it says.

Second: If an insurer is liable for a claim under an insurance policy *and* "is not in compliance with" the Act, it must pay, "in addition to the amount of the claim, interest on the amount of the claim at the rate of 18 percent a year as damages, together with reasonable and necessary attorney's fees." *Id.* § 542.060(a). And so, the standard for liability under section 542.060 is: (1) failure to be in compliance with the statute and (2) liability under the policy. Thus, setting aside whether there is liability under the policy, if the insurer is "in compliance" with the Act—whatever "in compliance" means—it does not have liability under the Act.

Thus, we must turn to determining what it means to "pay the claim" and be "in compliance" with the Act.

D. What does it mean to "pay the claim"?

1. The words of the Act.

Does "pay the claim" mean "pay the full amount ultimately determined by litigation, appraisal, or some other mechanism to be owed on the claim" *or* does it mean "pay the amount the insurer agrees is owed"? We believe it must mean the latter. All of the opinions handed down in *Barbara Technologies* presume it means the former. This, we are convinced, is an error; and one that carries significant consequences.

The steps an insurer must take to comply with the Act are these: (1) quickly acknowledge receipt of the claim, commence an investigation of the claim, and request information needed to evaluate the claim; (2) shortly after receiving whatever information is needed to determine coverage and the amount owed, tell the policyholder if the claim is being accepted or rejected; and (3) promptly after sending that notice, "pay the claim" if the insurer's coverage decision requires payment of the claim or any part of it. TEX. INS. CODE §§ 542.055, .056, .057.[10]

The Act should not be read, we think, to force an insurer to immediately pay an amount that it does not believe is owed under the contract, but is later determined to be owed through a process it does not control in which the ultimate decision is made by a third party. It is like requiring a person to pay the exact amount of a civil judgment before a lawsuit is filed. A person cannot presently comply with a requirement that is determined only by a future and uncertain event. The statutory language, in fact, recognizes that the requirement to pay is limited to those claims that the insurer acknowledges should be paid:

[10] The insurer also may ask for more "information" as it proceeds with its investigation (*see* TEX. INS. CODE § 542.055(b)), but asking for more information is not a step required for compliance with the Act.

> Except as otherwise provided by this section, *if an insurer notifies a claimant* under Section 542.056 *that the insurer will pay a claim or part of a claim*, the insurer shall pay the claim not later than the fifth business day after the date notice is made.

Id. § 542.057(a) (emphasis added). The payment deadline is conditioned on the insurer notifying a claimant that the insurer will pay. The other deadlines in the statute are similarly focused on insurer delays that have nothing to do with the merits of the claim, such as when the insurer has received all necessary documents and information. *See id.* §§ 542.055(a), 542.056(a). In other words, the statute prevents an insurer from simply sitting on a claim while a policyholder who has suffered a covered loss waits.[11]

There is a flow to the statute, with each step leading to the next. The obligation to "pay the claim" is an obligation to pay the amount the insurer has determined it is required to pay for the loss, less any deductible, depreciation, or other contractual offset. A penalty is assessed when the insurer fails to do this in a timely manner, not when an insurer fails to pay an unknown amount

[11] The policy necessity for this statute should be obvious. "Insurance companies make use of time value of money by earning investment income on premiums between the time of receipt and the time of payment of claims or benefits." *See* www.allbusiness.com/barrons_dictionary/dictionary-time-value-of-money-4942205-1.html (accessed September 5, 2019). The longer an insurer delays payment on claims, the more money it can make. This statute ensures that the cost of delaying payment will outweigh any potential business-side benefit of such a delay. *See also* www.irmi.com/term/insurance-definitions/time-value-of-money ("The longer the delay in making a payment, the more interest that can be earned.") (accessed September 5, 2019).

that is later established through a dispute-resolution process. Simply put, the Act concerns *payment*, not *coverage*.

Assume, as in the present case, the policyholder is seeking payment for repair of a storm-damaged roof on a commercial building. What if the insurance adjuster estimates the cost to remove and replace the old roof and the insurer pays that amount, but it is subsequently discovered that there were two hidden layers of old roofing to be removed, resulting in an additional cost? Should the insurer have liability under the TPPCA for underpayment of the claim that it accepted and paid to the extent reasonably possible at the time?

Even if the adjuster discovers all three layers of old roofing to be removed, her repair estimate may be different from the estimate made by the policyholder's engineer; and both of these estimates may be different from the amount ultimately charged by the roofing contractor who performs the work. The point, of course, is that the covered damage can be practically impossible to ascertain, and even if it is ascertained, the *exact* amount of money required to repair the damage is not always known with certainty. The best any insurer can be expected to do is to quickly conduct a reasonable investigation and promptly pay the amount that appears to be owed. And thats all the TPPCA requires.

Assume an insurance policy covers damages resulting from a storm-caused opening (which is now common for homeowners' policies) and the insurer has a legitimate reason to believe that a 25-year-old pitched roof is leaking rainwater because it is worn out (wear and tear being an excluded cause), not because wind forced rain uphill, under shingles, and into the structure. Consequently, the insurer denies an interior water-damage claim. Assume further that, two years later, a jury in the policyholder's lawsuit against the insurer is persuaded that wind, in fact, drove water uphill and into the house. Should the TPPCA punish the insurer for engaging in this legitimate, bona fide coverage dispute?

What if in a duty-to-defend context,[12] the insurer balks at high-priced lawyers retained by the policyholder? *See Lamar Homes, Inc. v. Mid-Continent Casualty Co.*, 242 S.W.3d 1, 19 (Tex. 2007) (applying the TPPCA to defense costs incurred in a third-party liability policy). If the insurer believes that defense counsel's hourly rate should be no more than $300 per hour in a given venue, but a jury subsequently finds that $375 per hour was reasonable, does the Court's interpretation of the TPPCA in the present cases require that the insurer

[12] Note that referencing *Lamar Homes* is not an indication that Texans for Lawsuit Reform concurs with the holding in that case.

be penalized with 18 percent interest for that difference, plus more attorney fees?

If the Court assumes "pay the claim" means "pay any amount that may later be determined to be owed under the insurance contract, well after the prompt pay deadline has passed," then the Act imposes strict liability for denial or underpayment of a claim. It imposes liability even when the denial or underpayment resulted from a legitimate dispute about coverage. It imposes liability for something that may not be subject to determination or exact quantification at the time of the prompt pay deadline. And it imposes liability for the failure of an early-stage estimate to exactly match a later-in-time decision by a third party. These are absurd results. *See Molinet v. Kimbrell*, 356 S.W.3d 407, 414–15 (Tex. 2011) (statutory construction should not lead to an absurd result); *Entergy Gulf States, Inc. v. Summers*, 282 S.W.3d 433, 437 (Tex. 2009) (same); TEX. GOV'T CODE § 311.021 (3), (4) (when interpreting Texas codes, it must be presumed that a just and reasonable result and that a result feasible of execution are intended). The TPPCA is to be liberally construed, but for one purpose: "to promote *the prompt payment* of insurance claims." *See* TEX. INS. CODE § 542.054 (emphasis added).[13] The purpose is not to provide a gotcha,

[13] In the Legislature's 2003 *non-substantive* re-codification of the Insurance Code, this provision was truncated from the previous version, presumably to eliminate unnecessary language. The previous version read, "This article shall be liberally construed to promote its

strict liability standard for claims that are impossible to fully evaluate at the onset. The purpose is not to punish bona fide disputes.

In fact, such a punitive statutory scheme is subject to strict construction. This Court has routinely protected its common-law obligation to disregard the Legislature's instruction to liberally construe statutes when the statutes are penal in nature. *See, e.g., Smith v. Sewell*, 858 S.W.2d 350, 354 (Tex. 1993) (refusing to follow the Legislature's mandate in Texas Government Code section 312.006(b) to liberally construe the revised statutes). "[I]t is recognized that if a statute creates a liability unknown to the common law, or deprives a person of a common law right, the statute will be strictly construed in the sense that it will not be extended beyond its plain meaning or applied to cases not clearly within its purview." *Id.* (citing *Dutcher v. Owens*, 647 S.W.2d 948, 951 (Tex. 1983) and *Satterfield v. Satterfield*, 448 S.W.2d 456, 459 (Tex. 1969)). The predecessor statutes to the TPPCA were recognized as penal in nature and strictly construed, and the present version of the Act is no less penal. *See, e.g.*,

underlying purpose which is to obtain prompt payment of claims made pursuant to policies of insurance." TEX. INS. CODE ANN. art. 21.55 (West 2003) (repealed). This previous version was clearer in respect to the limited scope of the article's purpose, that is, "*to obtain prompt payment* of claims made pursuant to policies of insurance." The purpose has never been to encourage insurers to abandon legitimate disputes in favor of payment.

McFarland v. Franklin Life Ins. Co., 416 S.W.2d 378, 379 (Tex. 1967) (construing now-repealed article 3.62 of the Insurance Code).[14]

If the Legislature intended to impose liability for underpayment of a claim (and denial of a claim really is just a form of underpayment), it would have written it into the Act. We know this because the Texas Insurance Code contains two other prompt payment of claims acts, one applicable to HMOs and another to PPOs. Both of these statutes specifically impose a penalty for underpayment of an insurance claim. *See* TEX. INS. CODE §§ 843.342(d)-(g), 1301.137(d)-(g). The TPPCA in Chapter 542 of the Insurance Code contains no similar language. In fact, it specifically acknowledges that a claim may be rejected or paid only in part. *See* TEX. INS. CODE § 542.057(a).

2. Other courts' interpretations of the Act.

Courts interpreting the TPPCA appear to agree that it is improper to interpret the Act to impose strict liability on the insurer based on a later-in-time determination that the insurer's payment was insufficient.

[14] In 2007, this Court recognized the Legislature's command to construe the TPPCA liberally, at least in respect to interpleaders *when the insurer acknowledged a payment obligation*. *See State Farm Life Ins. Co. v. Martinez*, 216 S.W.3d 799, 805 (Tex. 2007). While the TPPCA may be construed liberally in respect to prompt payment of *recognized* claims, it should be strictly construed in respect to its limited scope. The TPPCA was not intended to apply, and should not apply, to *disputed* claims.

In *Breshears v. State Farm Lloyds*, 155 S.W.3d 340 (Tex. App.—Corpus Christi 2004, pet. denied), an insurer paid $13,000+ on the insureds' claim under a homeowner's policy. The insureds, however, believed the claim was underpaid and filed a lawsuit against their insurer. The dispute went through the contractual appraisal process, resulting in a decision that the insurer had underpaid the claim. Even though the insurer paid another $5,700 within 30 days of the appraisal decision, the insureds maintained their lawsuit.

The insureds argued that because of the appraisal process, their claim was not actually paid until after the insurer paid them the difference between the initial payment and the appraisal award, which occurred long after the 60-day statutory limit provided by the TPPCA. The court of appeals disagreed. The claim was initially paid within the 60-day limit and "[t]he 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." This Court cites *Breshears* multiple times in its *Barbara Technologies* opinion, including to say that it "find[s] some of the reasoning in *Breshears* persuasive. *See Barbara Technologies Corp. v. State Farm Lloyds*, 2019 WL 2710089, at *11 (Tex., Feb. 20, 2019).

In *Mainali Corp. v. Covington Specialty Insurance Co.*, 872 F.3d 255, 259 (5th Cir. 2017), a fire damaged a commercial building owned by Mainali Corp.

Mainali filed claims with its property insurer, which paid the claims based on an independent adjuster's estimates. Mainali thought its claims were underpaid and sued the insurer. The dispute went through the contractual appraisal process, with the result being that the appraisal panel's award to Mainali was less than the insurer already had paid on the claims. The insurer, however, made a relatively small additional payment to ensure its payments were consistent with the way the appraisal panel allocated the losses.

Despite receiving more than the appraisers determined was due on the claim, Mainali sought to recover the statutory penalty and attorney fees from the insurer under the TPPCA, arguing that the insurer did not pay the claim within 60 days after the insurer received all documentation necessary to determine the amount owed on the claim. Relying on *Breshears*, the Fifth Circuit held there is no statutory violation of the TPPCA when the insurer's pre-appraisal payment is "reasonable." This Court cites *Mainali* with approval in *Barbara Technologies*. *See Barbara Technologies*, 2019 WL 2710089, at *12.

Earlier this month, in *Shin v. Allstate Texas Lloyds*, 2019 WL 4170259 (5th Cir., Sep. 3, 2019), the Fifth Circuit held that *Mainali's* "reasonableness" exception survives the decision in *Barbara Technologies*. The Fifth Circuit understands *Barbara Technologies*—when read in conjunction with *Mainali*—to provide that in order for an insurer to avoid liability under the TPPCA, the

insurer must have made a reasonable payment within the statutorily provided period.

In *Mainali*, the initial payment was "undeniably reasonable" because it exceeded the amount the appraisal panel found to be owed. In *Breshears*, the initial $13,000 payment was found to be reasonable even though the appraisal process ultimately required the payment of another $5,700. In *Shin*, the appraiser awarded almost $26,000, which was 5.6 times greater than the initial payment of about $4,600. Nonetheless, the Fifth Circuit determined that the insurer's initial payment was reasonable as a matter of law because: (1) the insurer "complie[d] with the TPPCA in responding to the claim, requesting necessary information, investigating, evaluating, and reaching a decision on the claim," and (2) the difference between insurer's initial payment and the appraisal determination was no larger than the difference found to be reasonable in other cases. *Shin*, 2019 WL 4170259, at *2 (citing *Hinojos v. State Farm Lloyds*, 569 S.W.3d 304, 307 (Tex. App.—El Paso 2019, pet. filed) (finding the insurer's initial payment was reasonable where the appraisal award was 6.8 times the initial payment, a difference of over $22,000)).

The deficiency in *Breshears*, we believe, is that it adds words to the TPPCA by holding that the statutory basis for imposing liability under the Act depends on whether there is "a reasonable payment within a reasonable time"—a

holding the Fifth Circuit has adopted. While we do not see support for a reasonableness exception in the plain language of the TPPCA, we agree with *Breshears*, *Mainali* and *Shin* to the extent the courts are concluding that the Act should not be interpreted to impose liability if the insurer timely pays the amount it has determined is owed and otherwise meets the Act's statutory deadlines.

3. In sum.

We believe the plain language of TPPCA requires an insurer to acknowledge and investigate a claim, notify the policyholder whether the claim will be accepted or rejected, and send the payment to the policyholder if part or all of the claim is accepted—all within statutory deadlines. Section 542.058 imposes liability only if the insurer fails to send the payment it agrees is due—fails to "pay the claim"—within the deadline provided. Section 542.058 does not impose liability for either underpayment or denial of a claim. In fact, the Act specifically allows partial payment and denial of claims. The Act itself explicitly states its purpose is "to promote the prompt payment of insurance claims," not to promote proper claims handling. *See* TEX. INS. CODE § 542.054. Liability for underpayment or rejection is provided by other laws, as discussed in Part F of this brief.

E. What does it mean to be "in compliance" with the Act?

Section 542.060 (the other liability section of the TPPCA) imposes liability on an insurer only if the insurer "is not in compliance with" the Act. The converse, therefore, is that if an insurer is in compliance with the Act, it does not have liability under the Act.

The steps required to be in compliance are these:

STEP 1: Within fifteen days after receiving notice of a claim, the insurer must (1) acknowledge receipt of the claim, (2) commence its investigation of the claim, and (3) request from the claimant all items, statements, and forms the insurer reasonably believes, at that time, will be required from the claimant. TEX. INS. CODE § 542.055(a).

STEP 2: Within fifteen business days of receiving whatever it needs (items, statements, forms or information) to determine coverage and the amount owed, the insurer must give the claimant written notice, either rejecting or accepting the claim. *Id.* § 542.056(a).

STEP 3: If rejection of the claim is the decision the insurer has made, it must state the reasons for rejecting the claim in the notice it sends under Step 2. *Id.* § 542.056(c).

STEP 4: If the insurer has accepted the claim in whole or part and given notice to the claimant that payment will be made, such payment must be made (*i.e.*, the insurer must "pay the claim" as discussed in Part D, above) not later than the fifth business day after sending the notice required by Step 2. *Id.* § 542.057(a).

The insurer *may be liable* under section 542.060 if it fails to comply with any of the deadlines or fails to provide an explanation for rejecting a claim.[15] But even if it fails to comply with the deadlines or fails to provide an explanation, it will owe damages under section 542.060 only if it is liable under the insurance contract. In other words, if an insurer does not owe any money under the contract, its failure to comply with the deadlines is irrelevant.

A decision tree would look like this:

- Did the insurer acknowledge receipt of the claim within 15 day of receiving the claim?

  _____ Yes _____ No

- Did the insurer commence an investigation of the claim within 15 days of receiving the claim?

  _____ Yes _____ No

- Did the insurer request from the claimant the items, statements, and forms it believes will be required to determine coverage and the amount owed under the policy within 15 days of receiving the claim?

  _____ Yes _____ No

[15] This provision complements the requirement that the insurer timely request all necessary documents to adjust the claim. An insurer should not be able to profess ignorance of necessary information as a reason to deny a claim, and a timely notice of reasons for rejection helps prevent such flimflam.

- Did the insurer notify the policyholder of its decision to either accept or reject the claim within 15 days of receiving the information it needs to determine coverage and the amount owed?

  _____ Yes _____ No

- If the insurer rejected the claim, did the insurer provide the reasons for rejecting the claim in the notice it sent the policyholder?

  _____ Yes _____ No

- If the insurer is accepting any part of the claim, did it pay the amount it has determined is owed within five days of sending the notice to the policyholder?

  _____ Yes _____ No

If the answer to all of these questions is "yes," then the insurer is "in compliance" with the Act and has no liability under section 542.060. If the answer to any of these questions is "no," then:

- Is the insurer liable to the policyholder under the insurance contract?

  _____ Yes _____ No

If the answer to this question is "no," then damages cannot be imposed against the insurer under the Act. If the answer is "yes," then the 18 percent statutory damages and attorney fees should be determined and awarded.

Note that our interpretation of "pay the claim" plays a role in determining liability under section 542.060, but is not the sole determinant like it is under section 542.058. Section 542.060 punishes the failure to meet the technical

requirements of the Act,[16] while section 542.058 creates liability specifically for failing to timely pay the amount acknowledged to be owed.

The Court recognizes that the Act includes both the express payment provision and other related provisions, but the Court's framing of the issue implies that the two are disconnected. *See Barbara Technologies*, 2019 WL 2710089 ("Though the TPPCA's purpose relates specifically to prompt *payment* of claims, the TPPCA also contains specific requirements and deadlines for responding to, investigating, and evaluating insurance claims."). In actuality, the additional requirements are part and parcel of effectuating the prompt payment of legitimate claims. Without these requirements, an insurer could delay payment by delaying the handling of the claim itself, whether it be with unscrupulous intent or mere failure to adequately staff its claims office, communicate with claimants effectively, or request sufficient documentation to inform a claims decision at the outset. The goal of the entire Act is to ensure prompt payment of legitimate claims.

[16] Consistent with the Act's purpose, such a technical violation would result in 18 percent penalty interest applied to the unnecessary delay caused by the insurer. An insurer who failed to staff its claim office adequately, causing a two-month backlog, would owe 18 percent interest for the approximate two months on each delayed claim.

F. When properly interpreted, the Prompt Payment of Claims Act fits neatly into Texas law.

Our construction of the Prompt Payment of Claims Act aligns it with the remainder of Texas law.

If an insurer denies or underpays a claim that is owed, the policyholder may pursue a breach of contract action to recover the amount owed under the contract, judgment interest, and attorney fees. The insurer does not need the TPPCA to provide a remedy for the wrongful denial of a claim or the underpayment of a claim, intentional or otherwise.

If an insurer acts badly in the claims-handling process, the policyholder has a remedy for that, too. The Unfair Claim-Settlement Practices Act provides that "it is an unfair method of competition or an unfair or deceptive act or practice in the business of insurance to engage in … unfair settlement practices with respect to a claim by an insured or beneficiary[.]" TEX. INS. CODE § 541.060(a). Unfair settlement practices include:

- failing to attempt in good faith to effectuate a prompt, fair, and equitable settlement of a claim with respect to which the insurer's liability has become reasonably clear;

- failing to promptly provide to a policyholder a reasonable explanation of the basis in the policy, in relation to the facts or applicable law, for the insurer's denial of a claim or offer of a compromise settlement of a claim;

- failing within a reasonable time to affirm or deny coverage of a claim to a policyholder; and

- refusing to pay a claim without conducting a reasonable investigation with respect to the claim.

Id. § 541.060(a)(2)-(7). Every action an insurer is required to take under the TPPCA also is mandated by the UCSPA. If an insurer conducted an insufficient investigation in order to underpay a claim (as opposed to merely delaying payment), it is subject to liability under the UCSPA. If an insurer denies a claim to avoid paying it, the insurer is subject to liability under the UCSPA. If an insurer fails to affirm or deny coverage within a reasonable time, the insurer is subject to liability under the UCSPA—even if there is no coverage. *See USAA Texas Lloyds Co. v. Menchaca*, 545 S.W.3d 479, 499–500 (Tex. 2018) (holding claims under the UCSPA are actionable even in the absence of coverage, if the policyholder suffers independent injury). The UCSPA allows for recovery without coverage, whereas in contrast, the TPPCA Act merely sets deadlines and imposes penalty interest, *but only if there is coverage*. *See* TEX. INS. CODE § 542.060(a). This limited remedy reflects the Legislature's intention not to capture improper claims handling—rather, only "the *prompt payment* of insurance claims." *See* TEX. INS. CODE § 542.054 (emphasis added).

In addition to fitting the TPPCA into the overall statutory scheme, our interpretation of that Act leaves the appraisal process undisturbed. The

insurance company either accepts and pays the claim, in whole or part, or rejects it in whole or part. (Again, we read the statute to equate payment to acceptance. Consequently, the failure to pay anything on a claim is a rejection of the claim for purposes of the Act, we believe.) If the insurer complies with the timing aspects of the Act along the way and pays the amount the insurer acknowledges is owed, then there is no liability *under the Prompt Payment of Claims Act*, no matter what subsequently happens in a dispute over the amount owed. If the parties find themselves in a disagreement about the amount of a claim, they may proceed through the appraisal process or to litigation. Either of these dispute-resolution mechanisms may or may not result in a payment by the insurance company to the policyholder. But either way, the TPPCA is not implicated retroactively. If the timing requirements of the Act are fulfilled, there is no liability under the Act regardless of the appraisal process. If the timing requirements of the Act are ignored, there may be liability under the Act no matter how the appraisal process is resolved.[17]

[17] The exception here would be if the appraisal process resolves the only issue in dispute between the parties. In such a situation, the appraisal award would constitute new information available to the insurer, the insurer would then acknowledge the amount owed, and the TPPCA would apply to the newly acquired documents and information to ensure payment was made promptly. But if a coverage disputes remains despite the appraisal award, the TPPCA would still not apply.

G. What are the consequences of the Court's interpretation?

The Prompt Payment of Claims Act, as interpreted by the Court, creates liability for statutory interest and attorney fees when it is determined months or years after the fact that an insurer underpaid a claim by a single dollar, regardless of the outcome of an appraisal. This can (almost certainly will) lead to the proliferation of lawsuits. Such a result could not possibly be the Legislature's intent.

Returning to one of the examples we provided above, if the insurer of a commercial building—*although acting in perfect good faith and meeting all other statutory deadlines*—fails to calculate the exact cost to replace the building's roof, it has, under the Court's opinion, failed to pay the claim within the deadline provided by the statute and is liable for statutory interest and attorney fees. Indeed, any insurer that fails to estimate with exact accuracy the amount owed to repair damaged property is liable for statutory interest and attorney fees. Similarly, an insurer that denies a claim because the alleged damages were not covered, or that found the covered damages fell within the deductible, also has liability if later determined to owe a single dollar on the claim. These insurers have no defense even though they are culpable of no actual wrongdoing. Liability for statutory damages and attorney fees is automatic when it is determined that the claim was underpaid, even by a single

dollar. *No matter how diligently an insurer acts, the insurer is at risk of being held liable for statutory damages and attorney fees.*

Moreover, if the insurer goes through the appraisal process and pays any additional amount found to be owed, the Court's decision still forces the insurer to go through litigation to defend its original valuation. *Under the Barbara Technologies holding, the insured will have been paid every cent owed under the insurance policy as determined by a neutral arbiter and still have the right to pursue a lawsuit to recover penalty interest and attorney fees.* Enterprising attorneys doubtless will see an opportunity to pursue a lawsuit in which the largest element of recovery will be attorney fees.

In the dispute between Barbara Technologies and State Farm, for example, State Farm *may have owed*[18] Barbara Technologies $178,845.25 on a commercial roof claim. The claim was first denied on November 4, 2013. According to the Court's reading of the TPPCA, the statutory damages at 18 percent per annum would begin to accrue 60 days later, on January 3, 2014. State Farm paid $178,845.25 on August 25, 2015. Therefore, under the Court's interpretation of the Act, State Farm might owe $52,830.40 to Barbara Technologies as penalty interest damages for this 599-day delay. But in reality,

[18] State Farm has never conceded that it owed the claim at all, much less over $178,000.

the amount found to be due through the appraisal process is not relevant to the subsequent lawsuit.

The Court has sentenced the parties to trial to determine if State Farm breached the parties' contract. Under the Court's interpretation, a jury will need to determine how much State Farm may have owed on the claim *in spite of* the appraisal. A jury could agree with State Farm's original valuation, in which case State Farm will escape liability. But the jury also could find that State Farm underpaid the claim by $1, $1,000, $100,000 or $1 million. Any of these findings will support a judgment forcing State Farm to pay penalty interest and Barbara Technologies' attorney fees, *on top of having already paid the claim in full as determined through the appraisal process*. The Court is not requiring Barbara Technologies to show that State Farm underpaid the claim by $178,845.25. All Barbara Technologies must do in the lawsuit this Court is allowing is show that State Farm failed to pay a single dollar on January 3, 2014, that was owed under the contract. Why would an insurer bother to go through the appraisal process or to pay an appraisal award if litigation over the issue is inevitable?

For every commercial insurance claim in Texas, there are dozens (maybe hundreds) of homeowner claims, each worth a fraction of what might be owed in a commercial case like *Barbara Technologies*. But the Court can rest assured that its interpretation of the TPPCA will incentivize some policyholder

attorneys to seek large awards of attorney fees for even small infractions. Some attorneys will chase pennies for their clients in order to recover tens of thousands of dollars for themselves. The quest for fees will be the driving force in many lawsuits. By making it difficult (if not practically impossible) for insurers to avoid liability under the TPPCA, the Court will give unscrupulous policyholder attorneys exactly what they what: an excuse to run up the bill.

As the Court notes, "[a]ccess to the appraisal process to resolve disputes is an important tool in the insurance claim context, curbing costs and adding efficiency in resolving insurance claims." *Barbara Technologies* slip op. at 11. "Appraisals can provide a less expensive, more efficient alternative to litigation." *In re Universal Underwriters of Texas Ins.*, 345 S.W.3d 404, 407 (Tex. 2011) (orig. proceeding) (citations omitted). Yet the Court's interpretation of the TPPCA neuters the appraisal process. Public policy encourages resolution of disputes through alternative methods, not the opposite. *See, e.g.,* TEX. CIV. PRAC. & REM. CODE § 154.002 ("It is the policy of this state to encourage the peaceable resolution of disputes . . . and the early settlement of pending litigation through voluntary settlement procedures.").

H. In closing.

We are convinced that the Court's reading of the Prompt Payment of Claims Act punishes engagement in a legitimate dispute about coverage and the

amount owed on a claim, requires a level of exactness in the claim-estimation process that is impossible to achieve, broadly construes the scope of the Act which is intended to be narrowly targeted, and will lead to the filing of unnecessary lawsuits, excessive legal fees, and an unnecessary cost to do business in Texas. Our reading of the Act, on the other hand, is faithful to the statutory language, does not lead to absurd results (in fact, the opposite), allows the appraisal process to continue to function to resolve claims, and allows the Prompt Payment of Claims Act to fit comfortably within the overall scheme of Texas law, including the Unfair Claim Settlement Practices Act. Adequate safeguards and penalties—those truly tied to bad actors—remain effective and in place. We urge the Court to reconsider its conclusion that the failure to "pay a claim" by the Prompt Payment of Claims Act deadline means the failure to pay every penny that ultimately is determined to be owed after a dispute is initiated.

Respectfully submitted,

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Certificate of Compliance and Service

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