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Appraisal Fundamentals In Modern Property Insurance Practice

By

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Introduction

The appraisal process can be a highly effective and efficient tool for both insurers and insureds in resolving disputes regarding the amount of loss or damage. While there is typically only modest variation among appraisal provisions found in modern property insurance policies, there are significant jurisdictional variations in the way in which such provisions are enforced and construed. Particularly in recent years, with the proliferation of claims arising from major Gulf Coast hurricanes, courts have been confronted with fundamental questions regarding the nature, scope, and purpose of appraisal. The decisions arising out of these cases have, in many instances, clarified the law of appraisal and provided needed guidance to parties seeking to use this important contractual right to resolve loss measurement disputes.

This paper will explore some of the "fundamentals" of appraisal including: (1) how various jurisdictions view the appraisal process (and whether and how they differentiate between "appraisal" and "arbitration"); (2) ways in which a party may waive its appraisal rights; and (3) the scope of issues that may be considered and/or determined by an appraisal panel. By highlighting different approaches to appraisal among various jurisdictions, this paper seeks to increase awareness of these issues and to engender a greater understanding of the legal framework under which appraisals operate.

I. Appraisal or Arbitration: What Is the Difference and Why Does It Matter?

Appraisal and arbitration are both methods of alternative dispute resolution employed in the insurance context. While these two processes share common features, including the avoidance of full blown litigation, most authorities agree that there are significant differences between them. Not all jurisdictions, however, have taken this view. In several states, appraisal is regarded as a form of arbitration. Even in states that have recognized some distinction between the two processes, courts sometimes use the terms "appraisal" and "arbitration" interchangeably, creating an element of uncertainty and confusion. Whether a proceeding is labeled an "appraisal" or "arbitration" is not merely a question of semantics. The way in which a court views the proceeding can have substantive implications with respect to its scope and the law governing its resolution.

While there are many definitions of the term "appraisal," the common denominator among them is the concept of valuation:

> **Appraisal,** *n.* (1817) **1.** The determination of what constitutes a fair price; valuation; estimation of worth. **2.** The report of such a determination. – Also termed *appraisement*. Cf. ASSESSMENT (3). – **appraise,** *vb.*[1]

As one court noted, "appraisal is primarily concerned with ascertaining the value of something."[2] In the insurance context, the term is generally associated with a form of alternative dispute resolution focused upon resolving disagreements between parties to an insurance policy regarding the valuation of the loss.

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[1] BLACK'S LAW DICTIONARY 117 (9th ed. 2009).

[2] *FTI Int'l, Inc. v. Cincinnati Ins. Co.*, 339 Ill. App. 3d 258, 260 (Ill. Ct. App. 2003).

Several authorities and courts have commented upon the characteristics that differentiate appraisals from arbitrations. As one leading insurance treatise observed, "appraisal is distinguished by its more limited role."[3] Whereas appraisers are focused on determining the amount of the loss or damage, reserving coverage issues for a court's determination, arbitrators' duties are broader in that they are often charged with resolving the entirety of the dispute between the parties:

> In the insurance context, appraisal is most often used to determine the amount of the loss sustained under a property insurance policy. Arbitration is a more far-reaching proceeding, by which the parties agree to have a neutral person or persons resolve a disputed matter.[4]

New York courts, among others, have distinguished appraisal from arbitration on this basis.[5] Further, some jurisdictions, which prohibit the arbitration of insurance disputes, have enforced appraisal provisions because their more limited scope has been found to preserve the court's jurisdiction by permitting litigants to test the award. For example, Louisiana's highest court has adopted this view.[6]

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[3] 15 COUCH ON INSURANCE 3d §209:8 (2005); *see also Merrimack Mut. Fire Ins. Co. v. Batts*, 59 S.W.3d 142, 149 (Tenn. Ct. App. 2001) ("Appraisal is something narrower. Appraisal is the act of estimating or evaluating something; it usually means the placing of a value on property by some authorized person.")

[4] 15 COUCH ON INSURANCE 3d at § 209:4.

[5] *Kawa v. Nationwide Mut. Fire Ins. Co.*, 174 Misc. 2d 407, 664 N.Y.S.2d 430, 431-32 (N.Y. Sup. Ct. 1997) (citing *In re Delmar Box Co., Inc.*, 309 N.Y. 60, 127 N.E.2d 808 (1955)) ("[A]rbitration . . . ordinarily encompasses the disposition of the entire controversy while appraisal extends merely to specific issues of cash value and the amount of loss, leaving all other issues for determination in a plenary action"); *see also In re Allstate County Mut. Ins. Co.*, 85 S.W.3d 193, 195 (Tex. 2002) ("while arbitration determines the rights and liabilities of the parties, appraisal merely 'binds the parties to have the extent or amount of the loss determined in a particular way'"); *Cas. Indem. Exch. v. Yother*, 439 So.2d 77, 79-80 (Ala. 1983) (distinguishing between arbitration and appraisal but declining to determine which type of provision was at issue in that case).

[6] *Sevier v. U.S.F.& G*, 485 So.2d 132, 136 (La. App. 2 Cir. 1986), *rev'd on other grounds*, 49 So.2d 1380 (La. 1986) ("We agree that mandatory *arbitration* vests the arbiter with the decision making power. However, *appraisal*, by definition, enables the court to inquire into the circumstances surrounding appraisal.")

Another difference between arbitrations and appraisals is that appraisals do not always share the "quasi-judicial" quality typical of arbitrations:

> [A]ppraisers are generally expected to act on their own skill and knowledge. They may reach individual conclusions and are required to meet only for the purpose of ironing out differences in the conclusions reached, and they are not obliged to give the rival claimants any formal notice or to hear evidence, but may proceed by ex parte investigation so long as the parties are given opportunity to make statements and explanations with regard to matters in issue. Arbitrators, on the other hand, must meet together at all hearings. They act quasi-judicially and may receive the evidence or views of a party to the dispute only in the presence, or on notice to, the other side, and may adjudge the matters to be decided only on what is presented to them in the course of an adversary proceeding.[7]

Courts in several states have focused on the quasi-judicial nature of arbitrations to distinguish them from appraisal proceedings.[8] In Florida, courts have looked to the level of formality of the proceeding called for by an appraisal provision to determine whether appraisal or arbitration was intended by the parties and whether state arbitration statutes govern a proceeding.[9] Interpreting an appraisal clause in *Allstate Insurance Co. v. Suarez*, Florida's highest court observed that "[i]t is clear from a plain reading of the clause that an informal appraisal proceeding, *not* a formal arbitration hearing" pursuant to a Florida arbitration statute was agreed upon by the parties.[10] The

[7] 4 AM. JUR. 2D *Alternative Dispute Resolution* §3 (2010).

[8] S*ee, e.g., IP Timberlands Op. Co., Ltd. v. Denmiss Corp.*, 726 So.2d 96, 105 (Miss. 1998) ("[A]rbitration presupposes the existence of a dispute or controversy to be tried and determined in a quasi judicial manner, whereas appraisement is an agreed method of ascertaining value or amount of damage.").

[9] *Allstate Ins. Co. v. Suarez*, 833 So.2d 762, 765 (Fla. 2002).

[10] *Id.*

court concluded that once a trial court determines that an appraisal clause has been invoked, subsequent proceedings cannot be conducted as arbitrations.[11]

It should be noted, however, that while many appraisals are less formal and do not resemble full-blown adversary proceedings, some may take on the quasi-judicial characteristics of an arbitration – particularly those involving large losses. A federal court sitting in New York recently declined to vacate an appraisal award despite the insured's argument that the proceeding had "morphed into an arbitration" as it involved the submission of thousands of pages of documents, the taking of seven witnesses' testimony, and legal briefing.[12] The award was confirmed on the grounds that the panel had stayed within the scope of its assignment to resolve "factual disputes over the amount of loss."[13]

Thus, while many jurisdictions have specifically concluded that appraisals do not constitute arbitration proceedings,[14] other states have obfuscated – or even eradicated – the distinction between them. As one commentator recently noted, the failure of the Arizona courts and legislature to address the distinctions between appraisal and arbitration in that state threatens to undermine a key goal of appraisal: the resolution of

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[11] *Id.*

[12] *Amerex Group, Inc. Lexington Ins. Co.*, 07 Civ. 3259 (HB), 2010 U.S. Dist. LEXIS 102098, at *7-9 (S.D.N.Y. Sept. 28, 2010).

[13] *Id.* at *8-9.

[14] *Hartford Lloyd's Ins. Co. v. Teachworth*, 898 F.2d 1058, 1062 (5th Cir. 1990) ("Under Texas law it is clear that an insurance appraisal which only determines the value of a loss is not an arbitration."); *Tamko Bldg. Prods., Inc. v. Factory Mut. Ins. Co.*, Case No. 4:09CV1401 CDP, 2009 U.S. Dist. LEXIS 121320, at *4-5 (E.D. Mo. Dec. 30, 2009) ("Traditionally, Missouri courts have distinguished arbitration and appraisal"); *Sun Microsystems, Inc. v. Electronic Servs. Inc.*, 25 Mass. L. Rep. 341, 2009 Mass. Super. LEXIS 95, at *11 (Mass. Super. Ct. Apr. 13, 2009) (concluding that appraisal provision did not constitute "arbitration" within the meaning of a state arbitration statute).

disputes without resort to litigation.[15] There is also a measure of uncertainty under Florida law regarding the nature of appraisals. While Florida has historically treated appraisal provisions as arbitration provisions,[16] the Florida Supreme Court held in *Allstate Ins. Co. v. Suarez* that the appraisal provision in that case was not an arbitration clause subject to state arbitration laws.[17] At least one court construing Florida law, however, appears to question the impact of *Suarez* regarding the applicability of arbitration statutes to appraisals.[18]

Still other states have determined that appraisals are a species of arbitration.[19] In Connecticut, for instance, it is well-established that appraisal provisions constitute agreements to arbitrate that are within the ambit of state arbitration statutes.[20]

A significant consequence of the manner in which a particular jurisdiction treats appraisal is the potential determination of which body or bodies of statutory law govern the proceeding. For instance, to the extent that a given jurisdiction views appraisal as arbitration, certain state and/or federal arbitration statutes may be found to apply. Notably, there are several states, including some that have adopted the Uniform

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[15] *See generally* Amy M. Coughenour, *Comment: Appraisal and the Property Insurance Appraisal Clause – A Critical Analysis: Guidance and Recommendations for Arizona*, 41 ARIZ. ST. L.J. 403 (2009).

[16] *E.g., Gray Mart, Inc. v. Fireman's Fund Ins. Co.*, 703 So.2d 1170, 1172 (Fla. Dist. Ct. App. 1997).

[17] *Suarez*, 833 So.2d at 765.

[18] *See Three Palms Pointe, Inc. v. State Farm Fire & Cas. Co.*, 250 F. Supp. 2d 1357, 1362 (M.D. Fla. 2003) (concluding that *Suarez* did not represent a change in Florida law with respect to the treatment of appraisals).

[19] *E.g.*, *Friday v. Trinity Universal of Kansas*, 939 P.2d 869, 871 (Kan. 1997) (holding that appraisal provision constituted an unenforceable arbitration provision under state law and observing that "[w]e do not see a meaningful distinction between appraisal and arbitration").

[20] *Giulietti v. Connecticut Ins. Placement Facility*, 534 A.2d 213, 217 (Conn. 1987); *see also Covenant Ins. Co. v. Banks*, 177 Conn. 273, 279-80 (1979) (minimizing any distinction between appraisal and arbitration and holding that state arbitration statutes apply to appraisal proceedings).

Arbitration Act, which apply state arbitration statutes to appraisal proceedings.[21] Other jurisdictions have expressly rejected this position.[22] Further, while some states appear to acknowledge differences between appraisal and arbitration, they nevertheless apply at least some statutory arbitration standards to appraisal.[23]

The possibility that the Federal Arbitration Act ("FAA") will govern an appraisal is also an important consideration. Several leading cases have held that "appraisal is not an arbitration and is not governed by the Federal Arbitration Act (FAA)."[24] However, the potential application of the FAA to an appraisal can be significant for a number of reasons, including that a court may decline to apply the FAA's presumption in favor of arbitration if the FAA does not apply.[25] Additionally, applying the FAA to appraisal proceedings could have an impact on procedural rules and protections otherwise available under state law to parties to an appraisal.[26]

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[21] *See Tamko Bldg. Prods., Inc. v. Factory Mut. Ins. Co.*, Case No. 4:09CV1401 CDP, 2009 U.S. Dist. LEXIS 121320, at *6 n.2 (E.D. Mo. Dec. 30, 2009) (citing cases).

[22] *Tamko*, 2009 U.S. Dist. LEXIS 121320, at *6 (holding that appraisal provision was not subject to Missouri's Arbitration Act and that the Act did not, therefore, bar the enforcement of the appraisal provision); *Rastelli Bros., Inc. v. Netherlands Ins. Co.,* 68 F. Supp. 2d 440, 446 (D.N.J. 1999) (holding that appraisals are not within New Jersey's Arbitration Act such that the Court must order that an appraisal proceed); *Suarez*, 833 So.2d 762, 765 (holding that the Florida Arbitration code was not applicable to appraisal proceedings).

[23] *See Quade v. Secura Ins.*, 792 N.W.2d 478, 483 (Minn. Ct. App. 2011) (dicta).

[24] *Dwyer v. Fidelity Nat'l Prop. & Cas. Ins. Co.*, 565 F.3d 284 (5th Cir. 2009) (*citing Hartford Lloyd's Ins. Co. v. Teachworth*, 898 F.2d 1058 (5th Cir. 1990)) (construing Standard Flood Insurance Policy according to federal common law and declining to apply the FAA's presumption in favor of arbitration).

[25] *Id.*

[26] *See Teachworth*, 898 F.2d at 1064 (observing that the misapplication of the FAA to an appraisal under Texas law had resulted in, among other things, the denial of the insurer's right to a jury trial on the validity of the award and the application of the wrong standards in assessing the validity of the award); *see also* Timothy P. Law & Jillian Starinovich, *What Is it Worth?: A Critical Analysis of Insurance Appraisal*, 13 CONN. INS. L.J. 291, 298 (2006/2007).

II. Use It or Lose It: the Potential Waiver of Appraisal Rights.

One of the most frequently litigated questions in the appraisal context is whether one party, either through its actions or inaction, has waived its contractual right to appraisal. A party seeking to avoid an appraisal may argue, for example, that the party demanding appraisal has forfeited its appraisal rights by delaying the demand for appraisal or opting to litigate the amount of loss. In some jurisdictions, courts have determined that a party may waive its right to appraisal if it maintains a position "inconsistent with the appraisal remedy."[27]

A. Timeliness of an appraisal demand

As is the case with many contractual provisions, a party may waive its rights under an appraisal provision by failing to invoke the provision in a timely manner. While some appraisal provisions may provide for a specific time period during which appraisal must be demanded, other policies may simply make appraisal available when the parties disagree as to the amount of loss or damage.[28] Where the policy does not specify a time limit for an appraisal demand, courts have generally concluded that such demand be made "within a reasonable period."[29] In a case involving a demand for appraisal in the context of the World Trade Center insurance coverage litigation, a federal court sitting in New York analyzed the following three factors in determining whether the timing of an appraisal demand was reasonable:

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[27] *Gray Mart*, 703 So.2d at 1172; *see also Dwyer*, 565 F.3d at 287 ("Like any other contract term, the appraisal provision may be waived by conduct inconsistent with invocation of the provision."); *Lundy v. Farmers Group, Inc.*, 750 N.E.2d 314, 319 (Ill. App. Ct. 2001).

[28] *But see Johnson v. Mut. Service Cas. Ins. Co.*, 732 N.W.2d 340, 346 (Minn. Ct. App. 2007) (holding that two-year suit limitation provision contained in a property policy applied to bar demand for appraisal).

[29] *E.g., SR Int'l Bus. Ins. Co., Ltd. v. World Trade Ctr. Props. LLC*, 01 Civ. 9291 (MBM), 2004 U.S. Dist. LEXIS 25642, at *9 (S.D.N.Y. Dec. 1, 2004).

> (i) whether the appraisal sought is "impractical or impossible" (that is, whether granting an insurer's appraisal demand would result in prejudice to the insured party); (ii) whether the parties engaged in good-faith negotiations over valuation of the loss prior to the appraisal demand; and (iii) whether an appraisal is desirable or necessary under the circumstances.[30]

The court in that case held that an insurer had not waived its appraisal rights, in part because the insured did not establish that the insurer's participation in the multi-party appraisal would be impossible or impractical. The court also found that good-faith negotiations regarding the amount of loss or damage were not a prerequisite to demanding appraisal.[31]

In analyzing the timeliness of an appraisal demand, it is critical to define the event or events that trigger a party's appraisal rights in the first instance. There is support in the case law for defining the triggering event as the moment at which the parties have "reached an impasse" with respect to the value of the loss.[32] Identifying the precise moment of "impasse", however, can be a difficult task, particularly when parties are in the midst of the adjustment process. A court's inquiry with respect to the timing of the impasse is often extremely fact-intensive and focuses on the specific conduct of each party.

Courts applying Texas law have recently decided several waiver cases employing the "impasse" standard. For instance, in In re Slavonic Mut. Fire Ins. Ass'n,

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[30] *Id.* at *9-10.

[31] *Id.* at *14-15.

[32] *Terra Indus. Inc. v. Commonwealth Ins. Co. of Am.*, 981 F. Supp. 581, 599 (N.D. Iowa 1997); *In re Slavonic Mut. Fire Ins. Ass'n,* 308 S.W.3d 556, 562 (Tex. Ct. App. 2010); *see also Tamko*, 2009 U.S. Dist. LEXIS 121320, at *8-10; *Newman v. Lexington Ins. Co.*, Civ. Action No. 06-4668, 2007 U.S. Dist. LEXIS 25141, at *11-13 (E.D. La. Apr. 4, 2007).

a Texas appellate court held that an insurer did not waive its right to appraisal in connection with a Hurricane Ike claim where the insurer demanded appraisal six days after receiving the insured's demand letter, which was served simultaneously with a lawsuit initiated by the insured.[33] The court rejected the insured's contention that the insurer knew of the "impasse" – and thus should have demanded appraisal – four months prior to receiving the demand letter, when the insurer informed the insured that it would not cover the cost of replacing an entire roof.[34] In that case, the insured did not respond to the insurer's denial of coverage until it served the demand letter and lawsuit. In another recent decision, a federal court applying Texas law declined to find that an impasse had occurred when the insurer reasonably believed that claim was settled or capable of being settled.[35]

Not all courts, however, have adopted the "impasse" standard for determining the time during which an appraisal demand must be made. For instance, Louisiana's highest court held that an insurer's demand for appraisal was not timely where the demand was not made within sixty days of receipt of a satisfactory proof of loss.[36] In that case, the court appeared to read the sixty-day limitation into the appraisal clause based, at least in part, upon the language of the statutorily sanctioned Louisiana

[33] *In re Slavonic Mut. Fire Ins. Ass'n,* 308 S.W.3d at 562.

[34] *Id.* at 562-63.

[35] *Tran v. Am. Econ. Ins. Co.*, Civ. Action H-10-0016, 2010 U.S. Dist. LEXIS 66283, at *7 (S.D. Tex. July 2, 2010) (finding that no waiver had occurred where insurer was not on notice that claim could not be settled until service of a lawsuit against the insurer and insurer's request for appraisal came within three months of this "impasse."); *but see Sanchez v. Prop. & Cas. Ins. Co. of Hartford*, Civ. Action No. H-09-1736, 2010 U.S. Dist. LEXIS 6295, at *14-17 (S.D. Tex. Jan. 27, 2010) (holding that an insurer's demand for appraisal was untimely where the insurer waited almost a year to invoke an appraisal provision from the time it received a call from the insured disputing the insurer's adjustment of a Hurricane Ike claim, during which time an unsuccessful mediation took place).

[36] *Sevier*, 485 So.2d at 1384.

standard fire policy which requires payment of claims within sixty days after "satisfactory proofs of loss."[37]

Finally, some jurisdictions require a party arguing that appraisal rights have been waived to establish that it was prejudiced by the other party's conduct.[38]

B. The decision to litigate

In some instances, a waiver of appraisal rights may be found where a party actively litigates the amount of the loss or damage. For instance, Connecticut's highest court held that by proceeding to trial upon the question of the amount of the loss, insureds waived their appraisal rights. The court therefore declined to disturb the jury's verdict, which denied damages to the insureds, on the grounds that their insurer refused to submit to an appraisal.[39] Similarly, a Florida court held that an insurer waived its right to an appraisal by "actively and aggressively litigating" its case for over fourteen months and by not demanding an appraisal until approximately one month prior to the scheduled trial of the case – after its motion for summary judgment had already been denied.[40] However, mere proximity to a trial date does not necessarily indicate that a waiver of appraisal rights has taken place. The Fifth Circuit Court of Appeals has rejected mere proximity between an insurer's request for appraisal and the trial date as grounds for finding waiver by an insurer, instead concluding that that the appropriate

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[37] *Id.* at 1383.

[38] *E.g., Rogers*, 984 So. 2d at 387-88.

[39] *Giulietti*, 534 A.2d at 217.

[40] *Gray Mart, Inc. v. Fireman's Fund Ins. Co.*, 703 So.2d 1170, 1171, 1173 (Fl. Ct. App. 1997); *see also Rogers v. State Farm Fire & Cas. Co.*, 984 So.2d 382, 387 (Ala. 2007) observing that waiver is established where a party "substantially invokes the litigation process and thereby substantially prejudices the party opposing [appraisal].")

waiver inquiry should examine when the insurer knew the appraisal clause could be invoked and whether the insurer reacted to this information in a timely fashion.[41]

III. Whose Job Is It, Anyway?: The Scope of Appraisal

In recent years, courts in various jurisdictions – especially states in the Gulf Coast region – have grappled with difficult questions regarding the appropriate scope of appraisal. Specifically, courts have been tasked with determining where an appraisal panel's work ends and where the function of the courts begins. While some jurisdictions limit the role of the appraisers to determining only the dollar value of the claimed loss, others have taken a more pragmatic view, allowing additional issues to be decided by appraisal panels.

There is general agreement that the role of an appraisal panel is to determine the amount of the loss, while coverage determinations are appropriately reserved to the courts for resolution.[42] As the U.S. Court of Appeals for the Second Circuit observed:

> It is well established that the scope of coverage provided by an insurance policy is a purely legal issue that cannot be determined by an appraisal, which is limited to factual disputes over the amount of loss for which an insurer is liable.[43]

However, the line between determining the amount of loss or damage and resolving questions of coverage is not as clear-cut as one might imagine. Straightforward loss determinations devoid of any complicating considerations are

[41] *Dwyer*, 565 F.3d at 288.

[42] *E.g., HHC Assocs. v. Assurance Co. of Am.*, 256 F. Supp. 2d 505, 511 (E.D. Va. 2003) (holding that "whether coverage was properly denied is a legal issue reserved for the court alone"); *Florida Ins. Guar. Ass'n, Inc. v. Olympus Ass'n, Inc.*, 34 So.3d 791, 794 (Fla. Dist. Ct. App. 2010) ("Issues relating to coverage challenges are questions exclusively for the judiciary.")

[43] *Duane Reade Inc. v. St. Paul Fire & Mar. Ins. Co.*, 411 F.3d 384, 389 (2d Cir. 2005); *see also Kawa v. Nationwide Mut. Fire Ins. Co.*, 664 N.Y.S.2d 430, 431 (N.Y. Sup. Ct. 1997) (holding that appraisal was inappropriate where the insurer contested liability for a windstorm loss).

perhaps the exception rather than the rule. Often, the matters requiring resolution are complex and nuanced, and can include multiple types of damage and/or the potential that multiple causes were involved in the loss. It is these types of situations that have forced courts to examine the parameters of an appraisal panel's role.

A major issue that has been the subject of several recent decisions is the extent to which an appraisal panel may consider loss causation in rendering a determination as to the amount of loss or damage. While courts have come down on both sides of this question, the balance seems to have swung in favor of allowing appraisers at least some discretion to consider causation. At the root of the causation question is whether causation is fundamentally an issue of liability (coverage) or damages in a particular case. As one court recently observed, "[c]ausation relates to both liability and damages because it is the connection between them."[44]

A. Cases barring consideration of causation issues by appraisers

Courts in several jurisdictions have attempted to draw rigid boundaries between the realm of appraisers (i.e., damages) and the realm of the courts (i.e., coverage) by disallowing any consideration of causation by appraisers. These courts have adopted a limited construction of the appraisers' obligation to determine the "amount of loss," holding that an appraiser's function is simply to render a value for the claimed loss.

Several courts have relied on the language of the appraisal provision - specifically, the term "amount of loss" - to determine the scope of the appraiser's task.[45]

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

[45] *Caribbean I Owners' Ass'n, Inc. v. Great Am. Ins. Co. of New York,* 619 F. Supp. 2d 1178, 1186-88 (S.D. Ala. 2008); *Wausau Ins. Co. v. Herbert Halperin Distrib. Corp.*, 664 F. Supp. 987, 988-89 (D. Md. 1987); *Rogers v. State Farm Fire & Cas. Co.,* 984 So.2d 382, 392 (Ala. 2007); *Merrimack Mut. Fire Ins. Co. v. Batts*, 59 S.W.3d 142, 149 (Tenn. Ct. App. 2001); *see Jefferson Ins. Co. v. Superior Court of Alameda Cnty.*, 3 Cal. 3d 398, (Cal. 1970) (interpreting term "actual cash value").

Alabama's highest court relied heavily upon this term, which it found to be unambiguous, in holding that "appraisers are not vested with the authority to decide questions of coverage and liability."[46] Defining "amount of loss" as the monetary value of the property damage, the court held that appraisal was inappropriate where the parties did not agree on the cause of damage to the insured property's brick veneer or foundation (which the insurer claimed was caused by excluded earth settlement), even though the parties agreed that the roof of the insured property sustained covered tornado damage.

Similarly, in several recent cases, federal courts construing Mississippi law have reaffirmed that state's long-standing position that "the purpose of an appraisal is not to determine the cause of loss or coverage under an insurance policy; rather, it is 'limited to the function of determining the money value of the property' at issue."[47] These cases go so far as to suggest that a resolution of coverage issues is a prerequisite to appraisal in Mississippi: "This Court 'must first determine the Policy's coverage of the losses and [the insurer's] liability for those losses, before the matter can be submitted for appraisal of the value of those losses.'"[48] Thus, a jurisdiction's reluctance to accept broader roles for appraisers may ultimately limit the utility and attractiveness of appraisal for parties in such jurisdictions.

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[46] *Rogers*, 984 So.2d at 392.

[47] *Jefferson Davis County Sch. Dist. v. RSUI Indem. Co.*, Civ. Action No. 2:08-cv-190-KS-MTP, 2009 U.S. Dist. LEXIS 16337, at *6 (S.D. Miss. Feb. 11, 2009) (quoting *Munn v. Nat'l Fire Ins. Co.*, 237 Miss. 641 (1959)); *Pearl River County Sch. Dist. v. RSUI Indem. Co.*, Civ. No. 1:08CV364HSO-JMR, 2009 U.S. Dist. LEXIS 80374, at *3-4 (S.D. Miss. Aug. 17, 2009); *see also Wells v. Am. States Preferred Ins. Co.*, 919 S.W.2d 679, 685 (Tex. Ct. App. 1996).

[48] *Pearl River County Sch. Dist.*, 2009 U.S. Dist. LEXIS 80374, at *4; *Jefferson Davis County Sch. Dist.*, 2009 U.S. Dist. LEXIS 16337, at *7-8.

B. Cases permitting consideration of causation issues by appraisers

While several jurisdictions have circumscribed the role of appraisers, others have recognized that considerations of causation are appropriate in an appraiser's determination of the "amount of loss," and that lines between liability and damages are not so neatly drawn.[49]

In several recent decisions, courts have reasoned that considering causation – at least to some extent – is actually a necessary component of an appraiser's task. In State Farm Lloyds v. Johnson,[50] the Texas Supreme Court observed that "[c]ausation relates to both liability and damages because it is the connection between them" and that appraisers must always consider causation, at least as an initial matter:

> 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 . . . But 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 . . .[51]

Thus, the Johnson court recognized that the facts of a given case generally determine which category "causation" generally falls into: "liability" or "damages." For instance, when different causes are alleged for a single injury to property, causation is a liability

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[49] *E.g., Secord v. Chartis Inc.*, 09 Civ. 9934 (SAS)(FM), 2010 U.S. Dist. LEXIS 139852, at *41 (S.D.N.Y. Dec. 8, 2010) (concluding that it is "clear under Connecticut law that appraisers may consider scope and causation in calculating the amount of a loss"); *CIGNA Ins. Co. v. Didimoi Prop. Holdings*, *N.V.*, 110 F. Supp. 2d 259, 268 (D. Del. 2000) ("[T]he court believes that under the circumstances of this case, including the plain language of the policy, a determination of amount of loss under the appraisal clause includes a determination of causation."); *North Carolina Farm Bureau Mut. Ins. Co., Inc. v. Sadler*, 693 S.E.2d 266, 269 (N.C. 2010), discretionary appeal allowed, 2011 N.C. LEXIS 30 (N.C. Feb. 3, 2011) ("It would be impractical for an appraiser to make a value determination for potentially insured damages without acknowledging the cause."); *see Augenstein v. Ins. Co. of N. Am.*, 360 N.E.2d 320 (Mass. 1977).

[50] 290 S.W.3d 886 (Tex. 2009).

[51] *Id.* at 892, 893.

question for the courts.[52] However, "when different types of damages occur to different items of property, appraisers may have to decide the damage caused by each before the courts can decide liability."[53] Further, under Johnson, it is always the job of appraisers to separate loss due to a covered event from a property's pre-existing condition.[54]

In Johnson, an insurer argued that appraisal was not appropriate in connection with a dispute regarding hail damage to a homeowner's roof because the parties' dispute concerned causation and not the "amount of loss."[55] While the insurer's inspector concluded that hail had damaged only the ridgeline of the roof, the insured's inspector concluded that the entire roof required replacement. Although the court questioned whether the dispute was related to causation in the first instance (as there was no dispute that the damage in question was caused by hail), it determined that the insurer could not avoid appraisal merely because there might be a causation question.[56] Several courts in other jurisdictions have relied heavily on the reasoning of the Johnson case.[57]

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[52] *Id.* at 892. It is on this basis that the *Johnson* court distinguished a Texas appellate court's decision in *Wells v. American States Preferred Insurance Co.*, 919 S.W.2d 679, 685 (Tex. Ct. App. 1996), in which the appraisers assessed foundation damage due to plumbing leaks (a covered peril) as "0" but damage due to settling (an excluded peril) as $22,875.94. *Id.*

[53] *Id.*

[54] *Id.* at 892-93.

[55] *Id.* at 888.

[56] *Id.* at 893.

[57] *E.g., Coates v. Erie Ins. Exchange*, 79 Va. Cir. 440, 444 (Va. Cir. Ct. 2009)(requiring an insurer to participate in an appraisal where the question was whether undamaged walls must be replaced in order to adequately fix an electrical system and return the premises to the pre-damaged condition).

In a recent decision involving a Hurricane Katrina loss, a federal court applying Louisiana law observed that, while "an appraiser's job is not to determine policy coverage or liability," causation must be considered in order to determine the scope of the loss that must be measured.[58] In that case, the court declined to set aside an appraisal award challenged by the insurer on the grounds that the appraisers made improper coverage determinations.[59] The court reasoned that there was no Louisiana authority standing for the proposition that appraisers may not make causation determinations, and even if there were, "[a]ny decisions of causation contained in the award may still be challenged, and neither [the insurer] nor the Court is bound by them."[60]

Florida has taken the position that causation is a question for the court in some circumstances, and for an appraisal panel in others. In Johnson v. Nationwide Mutual Insurance Co.,[61] Florida's highest court, resolving two conflicting lower court decisions, held that where an insurer contends that there is no covered loss, causation is an issue to be determined by the court. The court further concluded that causation issues are appropriately submitted to an appraisal where an insurer admits that there is at least some covered loss, but a disagreement exists as to the amount of the loss.[62] Thus, where the insured contended that its entire loss was caused by a sinkhole (a covered

[58] *St. Charles Parish Hosp. Serv. Dist. No. 1 v. United Fire & Cas. Co.*, 681 F. Supp. 2d 748, 757 (E.D. La. 2010).

[59] *Id.*

[60] *Id.*

[61] 828 So.2d 1021, 1025 (Fla. 2002).

[62] *Id.*

peril) and the insurer contended that the entire loss was caused by earth movement (an excluded cause), appraisal was found to be unavailable.

A Minnesota appellate court recently came to a similar conclusion, ruling that appraisal was inappropriate where there was a complete denial of liability for damage to roofs, and not merely a dispute as to the value or amount of the loss.[63] In that case, the parties disputed whether roof damage was caused by a storm or by inadequate maintenance of the insured property.

Conclusion

While general trends have emerged in appraisal jurisprudence, including the growing recognition that appraisals differ from arbitrations and the general application of the impasse/unreasonable delay standard with respect to determining whether a waiver of appraisal rights has taken place, there remain significant differences among jurisdictions, including whether and to what extent issues of causation may be considered. In order to ensure that appraisal is an effective and efficient method of alternative dispute resolution, parties must be aware of these differences and how they may ultimately affect the timing, scope, nature, and outcome of the process.

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[63] *Quade v. Secura Ins.*, 792 N.W.2d 478, 483 (Minn. Ct. App. 2011).