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INSURANCE LAW ALERT

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Ruling On Statutory "Bad Faith" Claim Following Appraisal Award Threatens The Appraisal Process

The role of appraisal as a means to resolve first-party property insurance claims has been the subject of some debate in Florida over the last several years. Appraisal provisions initially were incorporated into homeowners insurance policies in order to provide a means by which insurers and their policyholders could efficiently resolve disputes over the amount of a covered loss. The entry of an appraisal award is final and binding with respect to a first-party property insurance claim.

The Florida Supreme Court has deemed appraisal an informal process, leaving it lacking in structure and without a formal set of rules, as is in place for arbitration. Umpires are oft-times thought by both parties to have "split the baby," rather than to have rendered an independent determination as to the true amount of a covered loss. There also has been growing concern by insurers that the payment of an appraisal award may be considered a confession of judgment, leaving them exposed to "bad-faith" lawsuits. As a result of these uncertainties, the trend has been to remove appraisal provisions from insurance policies.

In response, the plaintiffs' bar and public adjusters have argued that insurers must be statutorily mandated to include appraisal provisions in their policies. They assert that removal of the provision would leave insureds unable to resolve property claims without protracted litigation. Removal of the provision also would impact public adjusters' business since the appraisal process affords them the opportunity to resolve claims on behalf of insureds, who may not yet be represented by counsel, providing them with greater control over the claims resolution process. In fact, in many cases, an insurer receives first notice of a disagreement as to the amount of a claim by way of an appraisal demand from their insureds'public adjuster.

Against this backdrop, the Florida Fourth District Court of Appeals, in the matter of *Trafalgar at Greenacres, Ltd. v. Zurich American Ins. Co.*, 2012 Fla. App. LEXIS 14869 (Fla. App. 4 Dist. Sept. 5, 2012), held that an appraisal award pursuant to an insurance contract constitutes a "favorable resolution" of an underlying breach of contract dispute for purposes of filing a bad faith action. The case, which arose from a claim for Hurricane Wilma damages to a shopping center owned by Trafalgar, was investigated by Zurich, which issued payments of $468,381.30 and $112,475.10 to the insured. A Sworn Statement in Proof of Loss in the total amount of $1,826,938.54 was submitted by Trafalgar, who then filed suit for breach of contract before Zurich completed its investigation. Zurich tendered an additional payment to Trafalgar and invoked appraisal under the policy.

An appraisal award ultimately was entered in the amount of $1,504,663.10. Zurich paid the balance within the requisite 30 days and sought to confirm the appraisal award. Zurich also sought and obtained summary judgment on Trafalgar's breach of contract action, but the trial court permitted Trafalgar to amend its complaint to assert a cause of action for statutory bad faith, alleging that Zurich engaged in a pattern of

delay and denial before and after litigation was filed. Zurich sought summary judgment on the bad faith claim, on the basis that Trafalgar had failed to obtain a "favorable resolution" of the underlying breach of contract claim. The trial court granted summary judgment in Zurich's favor, and Trafalgar appealed.

On appeal, the court found that because summary judgment on the breach of contract claim was based on Zurich's compliance with the terms of the policy *after* resolution of the appraisal process, Zurich had waived any defense to coverage by acknowledging and paying a loss amount to Trafalgar. The appraisal award resulted in a final determination of that loss amount. Finding no "meaningful distinction" between appraisal and arbitration, the court held that the appraisal award constituted a "favorable resolution" of an action for insurance benefits, satisfying the necessary prerequisite to an action for bad faith.

Although the *Trafalgar* decision is not yet final, it has garnered the attention of Florida's insurance community. At its core, it demonstrates a lack of understanding of the appraisal process and undermines the very reason for appraisal in the first instance, adding complexity and expense to a process which was conceived to timely resolve property claims while containing costs. If the decision stands, it inevitably will result in an increase in the removal of appraisal provisions from insurance policies, in order to avoid the risk of a bad faith lawsuit, triggering an increase in cries from the plaintiffs' bar and public adjusters to mandate appraisal by statute.

This additional risk of exposure to a suit for bad faith provides yet another avenue for insureds to seek extra-contractual damages in excess of an insurer's limits of liability. Its potential impact must be considered by insurers as they consider their approach to the resolution of first-party property insurance claims. ■

For more information about any of the topics covered in this issue of the Insurance Law Alert, please contact:

Susan Stryker, Esq.
sstryker@bressler.com
973.966.9681

Anna Lizette Flores, Esq.
lflores@bressler.com
954.430.7819

BRESSLER, AMERY & ROSS

A PROFESSIONAL CORPORATION

17 State Street
New York, NY 10004
212.425.9300

325 Columbia Turnpike
Florham Park, NJ 07932
973.514.1200

200 E. Las Olas Boulevard
Fort Lauderdale, FL 33301
954.499.7979

www.bressler.com