

Alert

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Global Insurance Alert

News Concerning Bad Faith and Extracontractual Issues

Fifth Circuit Reaffirms the Importance of a Reasonable Claim Investigation Prior to Denial

In *Santacruz v. Allstate Texas Lloyds, Inc.*, 2014 WL 5870429 (Nov. 13, 2014), the 5th Circuit allowed a policyholder to pursue a claim for common law and statutory bad faith even though the policyholder repaired the alleged damage before the insurer was able to observe that damage.

Factual Background

Mario Santacruz (the policyholder) purchased a homeowner's policy from Allstate Texas Lloyds, Inc. (the insurer). According to the policyholder, a rainstorm blew several shingles off the roof of his home, allowing water to enter the home and damage both the interior of the home and the policyholder's personal property. The policyholder reported the claim to the insurer the following day. However, the insurer stated that it would not be able to send an adjuster to the home for several days. The policyholder protested, as local weather called for additional inclement weather and a contractor had told him that tarps/patches would not protect the home from further damage. The insurer stated that policyholder should not make repairs until an adjuster was able to inspect the property. However, on the advice of the contractor, the policyholder repaired the roof.

Two days later, an adjuster arrived to perform an inspection. The inspector took photos of the interior and exterior of the home, but did no further investigation. The insurer denied the claim because the policyholder failed to provide access to the property. The insurer also contended that the repairs to the property prevented it from determining whether the rainstorm created an opening through which water entered the home, or whether the water penetration was due to other problems, such as wear and tear, deterioration or the weight of the rain.

Coverage Under the Policy

The policy contained two relevant provisions:

COVERAGE A (DWELLING)

We insure against physical loss to the property described in Coverage A (Dwelling) and Coverage B (Personal Property) caused by a peril listed below, unless the loss is excluded in Section I Exclusions.

3. Windstorm, Hurricane and Hail

This peril does not cover:

- b. loss caused by rain, snow, sand or dust, whether or not driven by wind, unless the direct force of wind or hail makes an opening in the roof or wall and the rain, snow, sand or dust enters through this opening and causes the damage.

CONDITIONS

3. Duties After Loss

- a. Your Duties After Loss. In case of loss to covered property caused by a Peril



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Insured Against, you must

- (5) as often as we reasonably require:
 - (a) provide us access to the damaged property.

The Ensuing Lawsuit

The policyholder filed suit, alleging that the insurer breached its common law duty of good faith and fair dealing. The policyholder also alleged numerous extracontractual statutory causes of action, but no cause of action for breach of contract.

The insurer filed a motion for summary judgment, arguing that the policyholder could not demonstrate that the rainstorm caused any opening to exist through which water might enter. The insurer argued that no evidence concerning the pre-storm condition of the roof existed, that no evidence showed that shingles were missing due to the direct force of wind and that no evidence foreclosed the existence of other, uncovered causes of loss. The insurer also contended that policyholder's decision to make repairs before an adjuster could inspect the loss violated the policyholder's duty to provide access as requested. The policyholder responded by filing an affidavit from his contractor in which the contractor averred that the damage was related to the rainstorm, as well as pictures, lists of personal property damaged, and cost of repair and replacement estimates. The policyholder also argued that interpreting the access clause as argued by the insurer would force him to violate his duty to mitigate the damage caused by the loss.

The trial court granted summary judgment to the insurer, holding that under *Universal Life Ins. Co. v. Giles*, 950 S.W.2d 48, 50-51 (Tex. 1997), bad faith only exists when an insurer has "no reasonable basis" for denying payment of a claim. In this case, the trial court ruled that the insurer's liability was never reasonably clear as significant questions existed as to whether policyholder's claim was covered by the policy. The trial court further held that the insurer's decision to deny the claim was reasonable given the evidence available at the time of the denial. Specifically, the making of repairs prior to inspection left open questions regarding whether the rainstorm caused an opening in the roof or whether other, uncovered factors, such as deterioration, wear and tear or the weight of the rain, allowed water penetration. As a result, the trial court held that the policyholder "has not carried his burden of proving the absence of a reasonable basis to deny his claim."

Appeal to the 5th Circuit

The policyholder appealed the summary judgment to the 5th Circuit, which reversed the trial court ruling. According to the 5th Circuit, an insurance company can deny a claim without acting in bad faith where a *bona fide* coverage dispute exists – the basis on which the trial court granted the insurer's summary judgment. However, the 5th Circuit also noted that an insurance company must reasonably investigate a claim and cannot conduct an investigation calculated to create a pretextual basis for denial. In this case, the 5th Circuit concluded sufficient evidence existed to allow a jury to find that the insurer did not conduct a reasonable investigation into the policyholder's claim. Although the 5th Circuit noted that the insurer's adjuster was on site two days after the claim was reported, the adjuster only took photos of the home in its post-repair condition. The adjuster did not speak with the contractor who repaired the roof, did not obtain weather reports concerning the storm in question, did not ask whether neighboring properties had suffered similar damage or take other steps to verify the policyholder's claim of covered damage. Stated differently, the insurer noted the lack of evidence regarding the cause of the damage after the repair, but did nothing to see if any secondary evidence could corroborate the claim for damage.

Implications

Santacruz highlights the importance of the underlying investigation, especially in a first party claim, in the decision to deny a claim. It appears that the investigation and documentation thereof is even more important when the basis for denial stems from a lack of information being provided by a policyholder. When the policyholder fails to provide information as requested, whether in terms of access to property or records, the insurer should consider whether or not corroborative evidence concerning the loss exists from secondary sources and can be reasonably obtained. If so, the insurer should attempt to gather, review and consider this secondary evidence. Otherwise,

according to the 5th Circuit, a decision to deny a claim can be challenged on the basis of an allegedly insufficient investigation separate and apart from the existence of a *bona fide* coverage dispute.

To discuss any questions you may have regarding the issues discussed in this Alert, or how they may apply to your particular circumstances, please contact Alicia Curran at (214) 462-3021 or acurran@cozen.com or Gregory Hudson at (832) 214-3909 or ghudson@cozen.com.