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Keeping Pace With Texas Hail Claim 'Case-Runners'

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Texas insurance carrier clients writing significant property insurance business in Texas all confirm a disturbing trend. Historically, Texas insurers have seen less than 2 percent of their property insurance claims result in a lawsuit. However, following Hurricane Ike, that figure jumped to almost 6 percent. But this increase pales in comparison to the exponential uptick in litigated claims Texas insurers are now experiencing in some parts of the Lone Star State. These insurers report that lawsuits have been filed in approximately 35 percent of all hail damage claims in Hidalgo County. One need only review the daily new lawsuit listings in Hidalgo County for corroboration.

Hidalgo County is not alone in this dramatic increase. Texas insurers note similar percentage increases in the number of lawsuits filed against insurers in Dallas, Tarrant and Potter Counties, also locations where hail events have occurred in recent years.

The ramifications of such statistics are self-evident. As the frequency of insurance claim litigation increases, insurance companies raise premiums to cover their costs. They also restrict coverage to address commonly litigated issues. Worst of all, some have decided to stop writing coverage in certain Texas counties altogether. The consequences to Texas policyholders and to the insurance industry as a whole are negative, as Texas consumers continue to pay the highest insurance premiums in the country as a result.[1]

So what explains this disturbing upward trend?

There are likely a number of converging factors.[2] But, one that deserves its fair share of the credit is the practice of “case-running” by public adjusters and other third parties involving themselves in the property insurance claim process. In short, case-running is the practice of seeking out, soliciting and referring policyholders with potential, albeit often questionable, property insurance claims to policyholder attorneys with the expectation of being compensated when the resulting litigation concludes.

Consider this scenario:

- A Texas homeowner submits a hail damage claim to its insurer. The claim is amicably resolved, a sworn statement in proof of loss is executed and the claim is paid.

- Six months later, a contractor knocks on the homeowner’s door. The contractor insists the homeowner’s claim was underpaid, that he has identified additional damage or, at a minimum, the insurer failed to pay “overhead and profit.” Seeing little downside, the homeowner signs a “contractor contingency agreement”

giving the contractor the right to present a supplemental claim to the insurer for additional damage and perform any additional work agreed to by the insurer.

- The contractor then advises that the homeowner will soon hear from a public adjuster who also helps with the supplemental insurance claim.

- Three days later, the public adjuster arrives at the home. The public adjuster brings out his iPad and captures the policyholder's electronic signature on, not one, but two separate contracts — his own contract for a 10 percent public adjusting services fee and a 30 percent contingent fee contract with an unfamiliar and absent policyholder attorney.

- Two weeks later, the insurer is served with a lawsuit filed by the policyholder attorney seeking damages for breach of contract, bad faith, statutory penalties and reasonable attorney's fees. Receipt of formal service of the lawsuit is the insurer's first notice of the supplemental claim and the policyholder's disagreement with its prior claim adjustment and payment.

- When the claim is resolved for nuisance value at an early mediation, the public adjuster takes his 10 percent fee, the lawyer takes his 30 percent fee and the contractor takes his $100 referral fee. The remainder is sent to the homeowner. No contracting work is ever completed on the home. No public adjusting services are ever provided.

And so describes the Texas hail claim case-running model. The contractor and public adjuster make a healthy living, not by providing legitimate services, but merely serving as a matchmaker between a Texas homeowner and a policyholder attorney.

It cannot be legitimately disputed that the increasingly common practice of case-running is in large part to blame for the increase in litigated insurance claims in Texas. Contractors and public adjusters subscribing to this approach have no intent to provide actual services in their client's best interest. Instead, it is all about extracting additional money from the insurance company.

So how can this be permissible? It isn't.

Texas attorneys are already subject to ethical and disciplinary rules, fee-sharing prohibitions and barratry laws that impose stiff penalties for participating in the improper solicitation of clients and the payment of referral fees to nonlawyers in exchange for client leads.[3] Accordingly, attorneys actively engaged in or benefiting from the practice of case-running are subject to civil liability, professional discipline, disbarment and even criminal prosecution.

But Texas' barratry laws also apply more broadly to other persons who, with the intent to obtain an economic benefit, solicit employment, either in person or by telephone, for themselves or for another, or accept or agree to accept money or anything of value to

solicit employment on an attorney's behalf. Thus, these prohibitions apply with equal force to contractors, public adjusters or other parties[4] engaged in case-running, and actual enforcement of these rules has gained some much-needed traction in recent years with several well-publicized criminal indictments.[5]

A number of states have also legislatively addressed inappropriate partnerships between public adjusters and policyholder attorneys in an effort to curtail the practice of case-running.[6] Unfortunately, Texas is not among them.

For example, under Louisiana law:

> A public adjuster shall not solicit employment for or otherwise solicit engagement, directly or indirectly, for or on behalf of any attorney at law, contractor, or subcontractor, in connection with any loss or damage with respect to which such adjuster is concerned or employed. Nothing in this Part shall be interpreted to prevent a public adjuster from recommending a particular attorney, contractor or subcontractor; however, the public adjuster is prohibited from collecting any fee, compensation, or thing of value for such referral.[7]

Similarly, under Virginia's insurance code:

> A public adjuster shall not refer or direct an insured needing repairs or other services in connection with a loss to any person in which the public adjuster has an ownership interest nor to any person who will or is reasonably anticipated to provide the public adjuster with any direct or indirect compensation for the referral of any resulting business.[8]

In addition to ongoing active enforcement of existing laws to penalize and deter this conduct, the Texas Legislature should take similar steps to specifically prohibit the practice of case-running by amending rules regulating the conduct of public adjusters. Adoption of statutory language along the lines adopted in Virginia and Louisiana would serve as a much-needed shot across the bow to those still engaged in the practice.

The ultimate goal of such legislative change would be to remove any incentive for public adjusters to enter contracts with policyholders if they have no intent to actually perform and document legitimate public adjusting services. Public adjusters serve a valuable role in the insurance claims process. Case-running for attorneys is not one of them.

Similarly, the Texas Legislature should consider the regulation of insurance restoration contractors. The multibillion dollar insurance restoration business is ripe for abuse and outright fraud. Each week, a Texas news agency reports on a contractor who "took the insurance money" and disappeared. Regulation of contractors engaged in the insurance restoration business could include prohibitions against case-running and other unethical behavior.

If the practice of case-running is not closely regulated, monitored and penalized, many

insureds will remain stuck in the middle of a framework where contractors and public adjusters merely act as referral conduits for policyholder attorneys and are rewarded for their illegal behavior. This arrangement neither reflects the value of services that legitimate contractors and public adjusters provide nor promotes a healthy environment for the resolution of valid insurance claims. It merely contributes to an exponential increase in the number of litigated insurance claims to the detriment of all Texas policyholders.

The bottom line? Keeping pace with Texas hail claim case-runners should continue to be a priority in Texas, particularly in the upcoming legislative session,

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[1] *Texas Homeowners Still Paying Nation's Highest Insurance Premiums*, Dec. 18, 2012, available electronically at http://www.dallasnews.com/news/state/headlines/20121218-texas-homeowners-still-paying-nations-highest-insurance-premiums.ece.

[2] For further discussion of factors driving up the number of disputed insurance claims in Texas, *see* Steven J. Badger, What the Hail is Going On in Texas?, Dec. 19, 2013, available electronically at http://www.zelle.com/news-publications-254.html, and Steven J. Badger, *The Emerging Hail Risk: What The Hail Is Going On*?, Claims Journal, May 2, 2014, available electronically at http://www.claimsjournal.com/news/national/2014/05/02/248354.htm

[3] Violation of Texas' criminal barratry statute, Texas Penal Code Section 38.12, is a felony of the third degree. Attorneys are also subject to the provisions of the Texas Disciplinary Rules of Professional Conduct §§ 7.01, 7.02 and 7.03 that prohibit improper solicitation of clients.

[4] These other parties might include unlicensed public adjusters, appraisers, consultants, general contractors, roofing contractors, restoration contractors or any other party engaged in seeking and soliciting clients on behalf of policyholder attorneys in exchange for an economic benefit.

[5] See, e.g., *Reynolds Faces More Barratry Allegations*, Mar. 25, 2013, available electronically at http://www.texastribune.org/2013/03/25/arrest-warrant-issued-rep-reynolds-barratry/; *Corpus Christi Attorney, Case Runner Sentenced on Felony Barratry Charges*, May 24, 2012, available electronically at

https://www.texasattorneygeneral.gov/oagnews/release.php?id=4056; and *Attorney and Community Activist Accused of Illegal Lawyering*, March 12, 2012, available electronically at http://www.chron.com/news/houston-texas/article/Attorney-and-community-activist-accused-of-3400059.php.

[6] *See* LA. REV. STAT. §22:1706.

[7] LA. REV. STAT. §22:1706(F).

[8] VA. CODE ANN § 38.2-1845.12 (2013).