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Breaking Apart the Perfect Litigation Storm

House Bill 3646 and Senate Bill 1628

by Kathleen Hunker, Policy Analyst

Background

Texas has some of the most expensive property insurance in the country, ranging from 20 to 50 percent higher than the national average in any given year.[1] A portion of this cost is a byproduct of the state's extreme weather patterns and excessive insurance regulation, but much can be blamed on enterprising attorneys who have created an entire cottage industry tasked with fermenting discord between insurers and their policyholders during the claims process.

To explain, a system of "case-running" has affixed itself to the insurance industry over the last few years, where public adjustors, among others, refer potential clients to attorneys, who then submit a large number of coordinated grievances against insurers. Very often these suits involve re-opened claims that had been previously settled, along with disputes over small discrepancies and those of otherwise dubious merit. The practice is particularly prevalent after wind and hailstorm damage. Indeed, as a result of this aggressive solicitation, the amount of hailstorm claims advancing to litigation leapt from 2 percent to 40 percent in some counties. Likewise, hail insurance claims have risen 84 percent statewide since 2010.[2]

Insurers have to expend resources to defend themselves against these additional demands, which not only adds to their overhead but also increases their liability risk. There would be nothing wrong with that if the claims were valid, but plaintiff attorneys usually bundle both meritorious and questionable claims of multiple clients into one big settlement offer. The heavy cost of defending each individual claims often leads to settlements in bulk on good and bad claims alike. Consequently, gratuitous litigation is raising the cost of insurance by millions of dollars, which will be paid by Texas families in the form of high premiums, increased deductibles, and the exclusion of hail damage from their policy's umbrella.[3] The pressure on insurers to shift these costs onto customers will only intensify as the cottage industry becomes more entrenched and begins to apply its strategy to other areas of the state.

Remove the Opportunity for Needless Litigation

As stated above, an increase in storm intensity cannot account for the explosion in alleged property damages nor the ratio of claims moving to trial. Rather, this is a result of exploitation of provisions of the Insurance Code that inadvertently create the perfect conditions for judicial rent-seeking.

State law currently imposes strict penalties on insurers if they deny or underpay a valid claim. This includes an 18 percent interest on the shortfall as well as the policyholder's attorney fees. The Texas Legislature enacted this rule in order to discourage insurers from rebuffing their customers in bad faith, but because Texas operates under "a day late or a dollar short" standard, even *de minimis* claims can rack up a hefty verdict, mostly in the form of court expenses, and the prospect of high fees could push the insurer to settle despite having a strong case. This guaranteed paycheck has given litigators both the opportunity and motive to exploit bona fide disputes for the sake of their firm's bottom line.

Accordingly, House Bill 3646 and Senate Bill 1628 adopt several approaches that remove an attorney's

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incentive to submit false, redundant, and/or negligible claims. For example, the proposed bills narrow the cause of action for a deceptive practice by limiting eligibility to a plaintiff who suffers "actual damage" and by explicitly excluding attorney fees from the definition of "actual damage." The bills also amend an insurer's general liability so that the company only need pay attorney fees when it "knowingly fails to act in compliance;" stated differently, a company would have to pay when it is not defending a bona dispute over the policy's terms.

In addition, both bills seek to eliminate lawsuits filed at eleventh hour, whereby contractors promise the insured a free roof if they sign over their right to negotiate the claim. Specifically, policyholders would have to submit written notice to the insurer, outlining the amount owed and the reasons why the damaged items were not previously submitted. Likewise, the insurer would disclaim liability if an appraisal results in a valid award that is consistent with the coverage and conditions provided with the policy. In this way, property owners obtain their contracted due, but the insurer also receives closure with respect to future claims on the policy.

Conclusion

Left unimpeded, the legal shakedown of Texas companies will reduce the accessibility of casualty insurance to ordinary Texans and bruise their ability to pursue property ownership. The decision to own property represents a decisive investment in someone's long-term financial wellbeing. At the same time, it requires a significant monetary commitment to purchase and maintain. This includes the cost of insurance, which gives Texans the necessary security in case the worst should happen.

Like all market services, however, the availability of insurance depends on price. We should not permit attorneys to swamp the system with false, redundant, and negligible claims and thus add to already high prices by increasing the risk that insurers have to underwrite. There are enough obstacles standing between Texans and property ownership without having to an attorney's billable hours to the mix. ✯

Notes

[1] Kathleen Hunker, *"Non-Renewal of Policies in Texas Homeowners Insurance Market,"* Texas Public Policy Foundation (2014), p. 2; Josiah Neely, *"Come Hail or High Water: Texas' Litigation Explosion,"* R Street Policy Study No. 31 (2015), p. 1.

[2] Josiah Neely, *"Come Hail or High Water: Texas' Litigation Explosion,"* R Street Policy Study No. 31 (2015), p.1-2.

[3] Steven Badger, *"The Emerging Hail Risk: What the Hail is Going On?"* Claims Journal (2014).

901 Congress Avenue, Austin, Texas 78701 | (512) 472-2700 PH (512) 472-2728 FAX | www.TexasPolicy.com