The Potential Liability of Insurance Adjusters Under the DTPA and the Texas Insurance Code

By Liz Brennan*

If you are a homeowner in Texas, you can probably empathize with the following situation. Imagine a husband and wife, joint homeowners, who uncover plumbing leaks throughout their house and the resulting cosmetic damage from these mysterious leaks. Having purchased an all-risks policy for their home, which insures homes against any losses not specifically included in a policy's coverage terms, they fully expect the water damage to be covered. They file a claim with their insurance company without any immediate problems. The insurance company hires an independent insurance adjusting firm whose private adjuster inspects the damage to the couple's house. The adjusters hire an engineering and consulting firm to further investigate and report on the cause of the leaks and damage to the home.

Much to the surprise of the homeowners, the engineering firm and the insurance adjusting firm conclude that only a minute portion of the cosmetic damage is attributable to plumbing leaks. Furthermore, the experts conclude that there is no foundation damage from the leak. The insurance company receives separate reports from the engineering and insurance adjusting firms and subsequently denies coverage for a substantial portion of the foundation damage.

The frustrated homeowners file suit against their insurance company, the independent insurance adjuster and the adjuster's firm. The claim alleges failure to promptly pay covered claims under Article 21.55 of the Texas Insurance Code (hereinafter "TIC"), failure to settle claims and unfair settlement practices under Article 21.21 of the TIC, and misrepresentations of coverage under the Deceptive Trade Practices Act (hereinafter "DTPA").

This article will examine the different avenues a homeowner may pursue when filing a lawsuit against an entity such as an independent insurance adjusting firm. Cases and statutes addressing insurance adjuster liability are not as clear as those concerning a homeowner's suit against his primary insurance company. Consequently, this article will take the road less traveled, and identify the pros and cons of suing an insurance adjuster under the DTPA and the TIC. In situations similar to the scenario above, a homeowner should consider the difficulties in bringing a lawsuit against an insurance adjusting firm or an insurance adjuster under the TIC. While suing the insurance company is an avenue for compensation, homeowners might choose to pursue the insurance adjuster who conducted the investigation. Filing claims against an independent adjuster or an adjusting firm under Article 21.55 of the code, which addresses prompt payment of claims, poses the issue of whether an insurance adjuster is considered to be "in" the business of insurance. Article 21.55 provides an extensive list of who is considered an "insurer" and defines an "insurer" as any entity or business that is authorized to act as an insurance company or to provide actual insurance.[1] This list establishes which entities fall under the provisions of Article 21.55 and, therefore, which businesses acting as insurance companies are expected to make prompt payment of claims to their insureds when necessary.[2] Unfortunately for homeowners faced with the reality presented above, the list does not mention any form of insurance adjuster or insurance adjusting firm, in-

dependent or otherwise.[3] Although the statute does not claim the list is exhaustive, it is fairly specific in enumerating the entities considered to be insurers. There is no mention of any type of insurance adjuster.[4] This exclusion leads one to believe that the list is fairly comprehensive and insurance adjusters were intentionally omitted from potential liability under Article 21.55.

Article 21.21, protecting against unfair methods of competition and unfair or deceptive acts or practices, may provide a homeowner's strongest claim against his insurance company for non-payment of claims. However, the process could prove to be complicated if the homeowner is pursuing a claim under Article 21.21 against an insurance adjusting firm or an insurance adjuster. Article 21.21 applies only to acts or practices in the "business of insurance." In *Dagley v. Haag Engineering Co.*, the Fourteenth Court of Appeals stated that the independent engineering company used to investigate claims in that case could not be sued under the provisions of Article 21.21 because the engineering company was not engaged in "the business of insurance," as that term should be defined for purposes of Article 21.21.[5]

A homeowner may also consider a claim against the adjuster based on a breach of the duty of good faith and fair dealing. This issue was addressed by the Texas Supreme Court in *Natividad v. Alexsis, Inc.*[6] In *Natividad,* the Texas Supreme Court held that an independent insurance adjuster does not owe a duty of any kind to an insured absent a contract, even if hired by the insured's primary insurance company.[7] The Dallas Court of Appeals in *Dear v. Scottsdale Ins. Co.* reached a similar conclusion, when it held that the independent insurance adjuster was not in privity of contract with the insured and, therefore, did not owe the insured any duty whatsoever.[8] The Fifth Circuit also affirmed the dismissal of a negligent investigation claim against an independent insurance adjuster in *Bui v. St. Paul Mercury Ins. Co.* because the adjuster was not a party to the insurance contract, and therefore was found to owe no duty to the insured under Texas law.[9]

While suing the insurance company is an avenue for compensation, homeowners might choose to pursue the insurance adjuster who conducted the investigation.

It follows from the above cases that an insurance adjuster does not owe an insured any contractual duties, and because it is not listed as an entity authorized to do business as an insurance company in Article 21.55, and may not be engaged in the business of insurance for purposes of Article 21.21. A rational conclusion may be reached that the ultimate responsibility falls with the primary insurance company from whom the insured bought his or her policy, not an independent adjusting firm hired for consulting purposes by the insurance company. Only if secondary contractual privity exists between an insured and an insurance adjusting firm, will there be the possibility of a claim based on the TIC or good faith and fair dealing.

In light of the inapplicability of claims under the Insurance Code, the DTPA may provide a more successful way of imposing liability on the adjuster. To maintain a claim under the DTPA, the homeowner must first show that he or she is a consumer as that term is defined in the Act.[10] Although there is no privity requirement under the DTPA, *per se*, the transaction complained of must form the basis of the homeowner's complaint, and the conduct complained of must have occurred "in connection with" the consumer's transaction. This judicial prerequisite to DTPA liability was imposed by the Texas Supreme Court in *Amstadt v. Brass Corp,* and must be satisfied whenever the consumer is not in privity with the defendant.[11] In *Amstadt*, the Texas Supreme Court held that a deceptive trade act or practice is not actionable under the DTPA unless it is committed in connection with a transaction involving goods or services.[12] Although there has not been much discussion of the "in connection requirement" since the decision in *Amstadt*, it probably requires that the adjuster's misrepresentations reach the homeowner to be actionable.

If the homeowners in the above situation can prove that any misrepresentations or unconscionable conduct arising out of the investigative services purchased by their insurance company, thereby satisfying the "in connection requirement," there is no requirement that the homeowner be the actual purchaser of the service. Services or goods purchased for the benefit of one party, even if actually bought by a third party, may form the basis for consumer status under the DTPA.[13] As the Texas Supreme Court held in *Kennedy v. Sale*, there is no indication in the DTPA that the legislature intended to restrict the application of the statute solely to deceptive practices committed by the person who actually furnished the good or service on which the complaint was based.[14] A plaintiff in a DTPA case establishes his or her standing as a consumer in terms of his or her relationship to the transaction, not by a contractual relationship with the defendant.[15]

A homeowner who files a claim against an independent insurance adjuster would be able to establish that he is a consumer under the DTPA. This is so even if the independent firm was hired by the homeowner's insurance company and not directly by the homeowner. Unlike the TIC, which is limited to the business of insurance, the DTPA applies to any service. Therefore, the DTPA appears to provide a more pragmatic method of recovering against an insurance adjuster for any misrepresentations or false claims made under the statute. Nonetheless, a lawsuit against a third party insurance adjuster by a homeowner has problematic areas, even under the DTPA.

The most serious problem homeowners will face in a DTPA suit against an adjuster was discussed in *Dagley v. Haag Engineering Co.*[16] If, as in *Dagley*, none of the insurance adjuster's representations concerning settlement of a homeowner's insurance claims are submitted directly to the homeowner, but instead are communicated directly to the insurance company, a homeowner will not be able to satisfy the *Amstadt* "in connection with" requirement.[17] The appellate court in *Dagley* also found that absent a special relationship between the third party investigative firm (here, an engineering company) and the insured, the adjuster could not be held liable for any alleged impropriety for its investigation into the insured's claims.[18]

The holding in *Dagley*, rested in part on the decision in *Dear v. Scottsdale Ins. Co.* wherein the court concluded that the insurance adjuster could not be held liable to the insured, regardless of how the insured phrased his complaints and claims against the adjuster.[19] The court in *Dear* stated:

> We also conclude that H & G, an independent adjusting firm hired exclusively by Scottsdale, had no

relationship with, and therefore owed no duty to, Dear. Absent such a relationship and concomitant duty, H & G could not be liable to Dear for improper investigation and settlement advice, regardless of whether Dear phrased his allegations as negligence, bad faith, breach of contract, tortious interference, or DTPA claims.[20]

A homeowner who chooses to pursue an insurance adjusting firm hired and controlled solely by the insurance company to investigate a claim is not likely to succeed in light of *Dagley* and *Dear*. However, if the homeowner can show enough communication or contact with the adjusting firm to prove that some or all of the investigative services were provided or communicated directly to the homeowner, rather than just for the insurance company, the homeowner's position would be significantly strengthened.

As noted above, another potential avenue for a homeowner bringing suit against an insurance adjuster is the unfair insurance practices section of the TIC, Article 21.21. In order to fall under the provisions of this article, the TIC requires that the act or practice complained of be in the "business of insurance."[21] Unfortunately for a homeowner looking to pursue an insurance adjuster for an unfair insurance practice claim, an independent insurance adjusting firm has a good argument to defeat a homeowner's claim pursuant to Article 21.21 because it can more easily allege that its conduct does not concern the business of insurance. In the *Dagley* case, the Fourteenth Court of Appeals concluded that the independent engineering company hired by the insurance company was not in the business of insurance as required by the TIC and, therefore, could not be held liable to the insured under Article 21.21.

> State Farm hired Haag to determine the extent of damage, if any, from the storm. Haag did not: (1) participate in the sale or servicing of the policies, (2) make any representations regarding the coverage of the policies, or (3) adjust any claims. As an independent firm hired to provide engineering services, it cannot be said that Haag is engaged in the business of insurance.[22]

Following this ruling concerning the liability of third party investigators under Article 21.21, an insurance adjusting firm could very well escape liability to a homeowner under the same principles, even if unfair practices were indeed committed by the adjuster. On the other hand, an adjusting firm might much more likely be considered in the business of insurance as opposed to an independent engineering firm such as the one in *Dagley*.

Entities and persons listed in Article 21.21 are prohibited from engaging in any deceptive trade practices set forth in the insurance code.[23] According to section 2 of Article 21.21, a "person" includes any individual, corporation, association, partnership, reciprocal exchange, inter-insurer, Lloyds insurer, fraternal benefit society, and any other legal entity engaged in the business of insurance, including agents, brokers, *adjusters*, and life insurance counselors."[24] The Texas Supreme Court in *Liberty Mutual Ins. Co. v. Garrison Contractors, Inc.* agreed that the definition of "persons" in Article 21.21 does indeed include insurance adjusters and adjusting firms.[25]

According to the *Natividad* case, an insurance carrier owes to its insured a non-delegable duty of good faith and fair dealing.[26] This duty arises from the nature of the contract between the two parties, which creates what the Texas Supreme Court in *Natividad* called a special relationship - one that arises due to the unequal bargaining power between an insurer and its insured.[27] Ultimately, a homeowner choosing to follow any of the courses of action presented in this article must remember that when his insurance company hires an outsider such as an insurance adjuster, the insurance company ultimately remains responsible for any and all breaches of duty.[28]

The options presented in this article are not exclusive remedies, and the position taken assumes that a homeowner is taking action directly against an insurance adjuster or adjusting firm. Articles 21.55 and 21.21 of the Texas Insurance Code and the Deceptive Trade Practices Act are the most likely avenues a homeowner and his lawyer would employ in the above situation. The most crucial point for a homeowner to remember is that Texas courts favor placing liability for both breaches of duty and mistakes made by an insurance adjuster on the homeowner's insurance company, regardless of which entity actually made the mistake.

According to the *Natividad* case, an insurance carrier owes to its insured a non-delegable duty of good faith and fair dealing.

* J.D. candidate, 2004, University of Houston Law Center, Chief Managing Editor, JOURNAL OF TEXAS CONSUMER LAW.

1. TEX. INS. CODE ART. 21.55 § 1(4) (2004), provides:

(4) "Insurer" means any insurer authorized to do business as an insurance company or to provide insurance in this state, including:

(A) a domestic or foreign, stock and mutual, life, health, or accident insurance company;

(B) a domestic or foreign, stock or mutual, fire and casualty insurance company;

(C) a Mexican casualty company;

(D) a domestic or foreign Lloyd's plan insurer;

(E) a domestic or foreign reciprocal or insurance exchange;

(F) a domestic or foreign fraternal benefit society;

(G) a stipulated premium insurance company;

(H) a nonprofit legal service corporation;

(I) a statewide mutual assessment company;

(J) a local mutual aid association;

(K) a local mutual burial association;

(L) an association exempt under Article 14.17 of this code;

(M) a nonprofit hospital, medical, or dental service corporation, including a company subject to Chapter 20 of this code;

(N) a county mutual insurance company;

(O) a farm mutual insurance company;

(P) a risk retention group;

(Q) a purchase group;

(R) a surplus lines carrier; and

(S) a guaranty association created and operating under Article 21.28-C or 21.28-D of this code.

2. *Id.*

3. *Id.*

4. *Id.*

5. Dagley v. Haag Eng'g Co., 18 S.W.3d 787, 793 (Tex. App.—Houston [14th Dist.] 2000, no writ). State Farm hired Haag to determine the extent of damage, if any, from the storm. Haag did not: (1) participate in the sale or servicing of the policies, (2) make any representations regarding the coverage of the policies, or (3) adjust any claims. As an independent firm hired

to provide engineering services, it cannot be said that Haag is engaged in the business of insurance.
6. Natividad v. Alexsis, Inc., 875 S.W.2d 695 (Tex. 1994).
7. *Id.* at 698.
8. Dear v. Scottsdale Ins. Co., 947 S.W.2d 908 (Tex. App. — Dallas 1997, writ denied).
9. Bui v. St. Paul Mercury Ins. Co., 981 F.2d 209, 210 (5th Cir. 1993).
10. *Dear*, 947 S.W.2d at 916-17; *see also Dagley*, 18 S.W.3d at 793.
11. Amstadt v. Brass Corp., 919 S.W.2d 644 (Tex. 1996).
12. *Id.* at 650.
13. Kennedy v. Sale, 689 S.W.2d 890, 892 (Tex. 1985).
14. *Id.* at 892.
15. *Id.*
16. Dagley v. Haag Eng'g Co., 18 S.W.3d 787 (Tex. App. — Houston [14th Dist.] 2000, no writ). The DTPA claims were based on Haag allegedly engaging in an unconscionable action or course of action; representing that its services were of a particular standard when they were of another, representing that its services have characteristics and/or benefits which they do not have, and representing that an agreement confers or involves rights, remedies, or obligations which it did not have.
17. *Id.* at 792.
18. *Id.*
19. Dear v. Scottsdale Ins. Co., 947 S.W.2d 908, 917 (Tex. App. —Dallas 1997, writ denied).
20. *Id.* at 916-17.
21. Tex. Ins. Code art. 21.21 § 2(a) (2004).
22. Dagley, 18 S.W.3d at 793. In *Dagley*, the plaintiffs also filed a claim based on negligence. The court dismissed this claim, noting that an essential element of negligence was a duty to the plaintiff and "Haag did not owe a duty to appellants in its investigation of their claims or providing evaluation materials to State Farm."
23. Tex. Ins. Code art. 21.21 § 1(a) (2004).
24. *Id.* at § 2(a) (emphasis added).
25. Liberty Mutual Ins. Co. v. Garrison Contractors, Inc., 966 S.W.2d 482 (Tex. 1998).
26. Natividad v. Alexsis, Inc., 875 S.W.2d 695 (Tex. 1994).
27. *Id.* at 698.
28. *Id.*