NO. 02-15-00328-CV

IN THE COURT OF APPEALS FOR THE SECOND DISTRICT
FORT WORTH, TEXAS

LON SMITH & ASSOCIATES, INC. and A-1 SYSTEMS, INC., D/B/A LON SMITH ROOFING AND CONSTRUCTION,

Appellants,

v.

JOE KEY AND STACCI KEY,

Appellees.

On Review from the 236th District Court of Tarrant County, Texas, Cause No. 236-267881-13, the Honorable Thomas Wilson Lowe, Presiding

BRIEF OF *AMICI CURIAE* NATIONAL ASSOCIATION OF PUBLIC INSURANCE ADJUSTERS and TEXAS ASSOCIATION OF PUBLIC INSURANCE ADJUSTERS IN SUPPORT OF APPELLEES

Steven J. Badger
State Bar No. 01499050
sbadger@zelle.com
ZELLE LLP
901 Main Street, Suite 4000
Dallas, Texas 75202
(214) 742-3000

Of counsel:

Brian S. Goodman
bgoodman@kg-law.com
Steven M. Klepper
sklepper@kg-law.com
KRAMON & GRAHAM, P.A.
One South Street, Suite 2600
Baltimore, Maryland 21202-3201
(410) 752-6030

Attorneys for Amici Curiae

Identity of Parties and Counsel

The identity of the parties to this appeal and their counsel are correctly set forth in their respective briefs. Amici curiae are:

National Association of Public Insurance Adjusters

and

Texas Association of Public Insurance Adjusters

Amici curiae are represented by:

Steven J. Badger
State Bar No. 01499050
sbadger@zelle.com
ZELLE LLP
901 Main Street, Suite 4000
Dallas, Texas 75202
(214) 742-3000

and

Brian S. Goodman
bgoodman@kg-law.com
Steven M. Klepper
sklepper@kg-law.com
KRAMON & GRAHAM, P.A.
One South Street, Suite 2600
Baltimore, Maryland 21202-3201
(410) 752-6030

Of Counsel

Table of Contents

Table of Authorities

Cases

Statutes and Rules

Other Authorities

Issues Presented

The National Association of Public Insurance Adjusters and Texas Association of Public Insurance Adjusters adopt the "Issues Presented" set forth in the Brief of Appellees.

Identity and Interest of *Amici Curiae*

The National Association of Public Insurance Adjusters ("NAPIA") is a nationwide trade association of public insurance adjusters organized in 1951 to professionalize the growing profession of public adjusting. NAPIA exists for primary purposes of professional education, certification, legal and legislative representation, scholarship and research, and marketing and promotion of the public insurance adjusting profession. NAPIA assesses its member firms annual membership fees to help further these several goals.

NAPIA's interest in the outcome of this appeal is a substantial and direct one. For over 60 years, NAPIA has worked closely with the insurance industry, state insurance departments, state governors and legislators, and attorneys general to ensure that public adjusters – the only professionals specifically licensed and regulated to prepare first-party insurance claims on behalf of a consumer or commercial insured – practice their profession in an ethical and accountable way.

The Texas Association of Public Adjusters ("TAPIA") is a statewide trade association of public insurance adjusters organized in 1990 to elevate the growing profession of public insurance adjusting in the State of Texas. TAPIA's primary function is professional education, legal and legislative representation, and the marketing and promotion of the public insurance adjusting profession. Important in TAPIA's mission is the eradication of the unauthorized practice of public adjusting

to assure that consumers in Texas are represented by only those individuals who are qualified, and licensed, to do so. TAPIA funds its activities through membership dues, and fundraising for specific legislative or legal initiatives.

Consistent with its core objectives, NAPIA filed an amicus curiae brief in the United States Court of Appeals for the Fifth Circuit, successfully urging the affirmance of the decision in *Reyelts v. Cross*, 968 F. Supp. 2d 835 (N.D. Tex. 2013), *aff'd*, 566 F. App'x 316 (5th Cir. 2014). The federal courts there held that Lon Smith & Associates, Inc. and A-1 Systems, Inc. d/b/a Lon Smith Roofing and Construction ("Lon Smith") violated Section 4102.051(a) of the Texas Insurance Code, under which a "person may not act as a public insurance adjuster in this state or hold himself or herself out to be a public insurance adjuster in this state unless the person holds a license or certificate issued by the commissioner," by contracting to provide unlicensed public adjusting services. NAPIA firmly believes that Lon Smith's actions in this case are flouting Chapter 4102 and the judgment against it in *Reyelts*.

For reasons explained further below, NAPIA and TAPIA (collectively "*Amici*"), including their individual public insurance adjuster members, have a strong interest in ensuring that statutes like Section 4102.051 are enforced to prevent roofers and other contractors from acting or contracting to act as public insurance adjusters without being licensed as same. Enforcement of statutes like

Section 4102.051 of the Texas Insurance Code prohibiting the unlicensed practice of public adjusting not only protects the licensed public insurance adjuster profession, but also protects homeowners from financial conflicts of interest when unlicensed and sometimes unscrupulous contractors purport to act as intermediaries with insurance companies on behalf of homeowners, just as Lon Smith did in this case.

Source of Fee

Amici are paying all fees incurred in preparing this brief.

Statement of Facts

Amici incorporate the "Statement of Facts" in the Brief of Appellees.

Summary of Argument

Strong public policy concerns support class-wide relief to enforce Section 4102.051(a) against Lon Smith. The contract gave Lon Smith a full obligation and full authority to negotiate directly with the Keys' insurance company with respect to the "final contract price" that the insurance company would pay for the storm damage to the Keys' roof. Allowing unlicensed intermediaries between the homeowner and an insurance company would wreak havoc on the licensed and regulated public insurance adjuster profession and would allow contractors to take advantage of homeowners – particularly in the face of a catastrophic natural disaster, when they are the most vulnerable – in situations where the contractors' financial interests obviously conflict with those of the homeowner.

A class action is a superior means of bringing relief to thousands of Texans whom Lon Smith duped into signing illegal contracts. Roofing contractors are particularly problematic, and the judicial findings of fact in *Reyelts* show that Lon Smith is representative of the typical contractor engaged in this illegal conduct.

Class relief is necessary to bring an end Lon Smith's illegal conduct and properly compensate its victims.

Argument

I. The public interest favors swift and comprehensive relief for thousands of Texans whom Lon Smith signed to illegal contracts.

Forty-five states, plus the District of Columbia, have enacted comprehensive licensing statutes regulating public insurance adjusters. These statutes address directly the problems inherent in allowing contractors or other unlicensed individuals or entities to act as unlicensed public adjusters. For example, in addition to prohibiting unlicensed contractors from practicing public adjusting, Texas law prohibits licensed public insurance adjusters from conflicts of interest and from soliciting homeowners during natural disasters, among other things. *See*, *e.g.*, TEXAS INS. CODE §§ 4102.151–4102.158. Additionally, licensed public insurance adjusters are subject to a code of ethics, TEXAS INS. CODE § 4102.005, hold funds for their clients in a fiduciary capacity, TEXAS INS. CODE § 4102.111, have limitations on commissions and fees that can be earned, TEXAS INS. CODE § 4102.104, and face administrative penalties for improper conduct. TEXAS INS. CODE § 4102.201

There are no such rules of conduct or ethical guidelines for contractors soliciting homeowners after catastrophic events. Roofing contractors are not even required to obtain a license to operate in Texas. Fraud and other impermissible conduct is widespread and sadly on the rise. *See* Dave Lieber, *Watchdog: Let's rein*

in dishonest roofing contractors, DALLAS MORNING NEWS, Dec. 31, 2015, http://goo.gl/P9xFG4.[1]

In 2005, the Texas Legislature enacted the Texas Public Insurance Adjusting Licensing Act, set forth at Chapter 4102 of the Texas Insurance Code, to protect Texans from the precise sort of predatory practices that the Keys encountered here. Shortly before the enactment of Chapter 4102, a court described how California's similar act protected policyholders from exploitation in times of crisis:

> [T]he [California] Legislature recognized that insureds would often be susceptible to exploitation in the wake of earthquakes, fires, floods, and similar catastrophes and that consumers of public adjusting services needed protection. In addition to price gouging and collusion with contractors, the Public Adjusters Act protects California consumers from a number of other abuses including high-pressure sales tactics, fraud, and incompetence. To ensure accountability and compliance with professional standards already in place for adjusters employed by the insurers, the Legislature included the licensure requirement as a part of the statutory scheme. In light of the consumer protection goals of the statute as a whole, we infer that the licensure requirement was aimed at any firm that might potentially exploit insureds in a vulnerable position by offering to help them through the insurance claim ordeal.

[1] A similar class action was recently filed against another North Texas contractor. The class representative in that matter is Ambrocia Ortega, a 93 year old widow living in the Oak Cliff neighborhood of Dallas. After a hail event, Ms. Ortega signed a contract with a roofing contractor which stated that the contractor would file an insurance claim and that "[a]ll negotiations and servicing responsibilities will be handled by contractor." The contractor received the insurance proceeds, but never installed a new roof. The number of class members is believed to be in the thousands. *See Ortega vs. Jorge Garcia, et al.*, No. DC-15-03338; 134th District Court, Dallas County (filed April 5, 2016). The class members in that matter are being represented by counsel for *Amici*, Zelle LLP.

Bldg. Permit Consultants, Inc. v. Mazur, 19 Cal. Rptr. 3d 562, 571 (Ct. App. 2004). The Texas statute expressly stated what the California courts found to be implicit: a contract that violates the public adjusters act "may be voided at the option of the insured." TEX. INS. CODE § 4102.207(a).

Because laws cannot enforce themselves, banning a predatory practice isn't the same as eradicating it. Seven years after the enactment of Chapter 4102, the Texas Insurance Commissioner reported that the unlicensed practice of public adjustment remained a serious problem: "a number of contractors, roofing companies, and other individuals and entities not licensed by the department have been advertising or performing acts that would require them to hold a public insurance adjuster license." Tex. Dep't of Ins., Commissioner's Bulletin #B-0017-12, June 26, 2012. The "tactics used by these unlicensed individuals include visiting neighborhoods and areas of the state where languages other than English are commonly spoken. These unlicensed individuals often prey on unknowing consumers by promising to 'work' insurance claims to achieve a higher settlement." *Id*.

Lon Smith is a perfect example. In *Reyelts*, Judge Cureton found (and the Fifth Circuit affirmed) that Lon Smith violated four different consumer statutes in deceiving a retired schoolteacher. 968 F. Supp. 2d at 839. Lon Smith showed up

after a hailstorm to offer its roofing surfaces. *Id*. Just like the Keys' contract,[2] the Reyelts' contract provided:

> This Agreement is for FULL SCOPE OF INSURANCE ESTIMATE AND UPGRADES and is subject to insurance company approval. By signing this agreement homeowner authorizes Lon Smith Roofing and Construction ("LSRC") to pursue homeowners['] best interest for all repairs, at a price agreeable to the insurance company and LSRC, and at NO ADDITIONAL COST TO HOMEOWNER EXCEPT THE INSURANCE DEDUCTIBLE AND UPGRADES. The final price agreed to between the insurance company and LSRC shall be the final contract price.

Id. The insured agreed to pay Lon Smith $14,775.48 for roof repairs, plus $1,176.00 in alleged upgrades, and Lon Smith agreed it would handle everything with her insurer. *Id*. at 840. Instead, Lon Smith completed the roofing work without ever contacting the insurer, much less attempting to negotiate a price. *Id*. at 840–41.

When Lon Smith pressed the retired schoolteacher for payment of the $1,176.00 in upgrades, she said she could not verify whether the work was done. *Id*. at 841. Lon Smith suggested that she "climb onto the roof and inspect the roof herself." *Id*. Because age and physical limitations prevented her from doing so, the insured relied on Lon Smith's representations. *Id*. One month after she tendered payment, Lon Smith demanded the $14,775.48 repair price and threatened "further collection activity" if she didn't pay. *Id*. at 842. The insured, upon calling her insurer

[2] The only difference is that the Keys' contract omits the phrase "at NO ADDITIONAL COST TO HOMEOWNER EXCEPT THE INSURANCE DEDUCTIBLE AND UPGRADES" appearing in the Reyelts' contract. That additional language is not relevant to whether the contract violates Chapter 4102.

to find out why it hadn't paid the $14,775.48 balance, learned that Lon Smith never contacted her insurer. *Id*. In fact, the insurer proceeded to deny coverage for the repairs because it had no opportunity to evaluate the loss. *Id*. Judge Cureton ruled that, under Chapter 4102, Lon Smith's contract was "illegal in its entirety, void and unenforceable," and that the insured was entitled to return of the entire $1,176.00 she paid Lon Smith. *Id*. at 843, 846.

Unrepentant and contrary to the *Reyelts* decisions, Lon Smith argues the Keys do not even state a plausible claim for relief in alleging that Lon Smith's form contracts with thousands of Texans violate Chapter 4102. Obviously, Judge Cureton's ruling, affirmed by the Fifth Circuit, is at least sufficient for the Keys to state a claim, whether or not that ruling is *res judicata* against Lon Smith. As Lon Smith's brief shows, it is taking a "kitchen sink" approach to obfuscate the obvious point that a roofing contractor who receives "authoriz[ation] to pursue homeowners['] best interest for all repairs, at a price agreeable to the insurance company and [the contractor]," as Lon Smith did in the Keys' contract, is "act[ing] on behalf of an insured in negotiating for or effecting the settlement of a claim or claims for loss or damage under any policy of insurance covering real or personal property." TEX. INS. CODE § 4102.001(3)(a)(i).

It is with good reason that, under Texas law, a licensed public adjuster "may not . . . participate directly or indirectly in the reconstruction, repair, or restoration

of damaged property that is the subject of a claim adjusted by the license holder." TEX. INS. CODE § 4102.158(a)(1). The inherent conflict of interest in allowing an unlicensed and unregulated contractor performing the repair work to negotiate the final price that the insurance company will pay for its work is insidious and inescapable. Roofing contractors present a particular problem. Tex. Dep't of Ins., Commissioner's Bulletin #B-0017-12, June 26, 2012; *see* TEX. INS. CODE § 4102.163.[3] Roofing work is rife with the potential for abuse, given most homeowners' inability or reluctance to climb onto their roofs to inspect the damage or the repairs. *Reyelts*, 968 F. Supp. 2d at 841. The public interest strongly favors swift and comprehensive action relief for the thousands of Texans hurt by Lon Smith's illegal contracts.

II. A class action is superior to other methods of adjudication.

Amici will focus on why class-wide adjudication is, as a public policy matter, "superior to other available methods for the fair and efficient adjudication of the controversy" under Rule 42(b)(3) of the Texas Rules of Civil Procedure.

[3] In 2013, the Texas Legislature enacted a second statute addressing the problems associated with contractors acting as unlicensed public insurance adjusters. Effective September 1, 2013, this new statute clarified existing law by categorically stating that roofing contractors were prohibited from holding public insurance adjuster licenses. TEX. INS. CODE § 4102.163. Although that law was not in effect at the time of the Keys' 2011 contract with Lon Smith, Texas law already prohibited any person from serving as both contractor and public insurance adjuster on the same claim. TEX. INS. CODE § 4102.158(a)(1).

Lon Smith wants to require each and every homeowner to bring suit separately and individually under each contract. Its "kitchen sink" brief is a strong indication of the time and effort that each insured would need to undertake to recover damages that – although significant to ordinary Texans – are relatively paltry in the world of civil litigation. In *Reyelts*, it took the insureds over two years of federal litigation to recover damages that, with non-economic damages of $30,000, totaled $31,176. 968 F. Supp. 2d at 847. Because they also proved the violation of debt collection statutes and the Texas DTPA, the homeowner also recovered their attorneys' fees, which totaled nearly $200,000. *Id*. at 851.

Not all victims, however, have the type of additional causes of action and other damages that would make it economically feasible to pursue individual claims when faced with such scorched-earth tactics. The Keys seek to represent a class of individuals who do not have (or do not wish to pursue) such larger individual claims. The class seeks only the return of amounts paid to Lon Smith under the illegal contracts. Anyone who wishes to pursue such a larger claim may of course opt out.

Most significantly, just last week the Fifth Circuit cited the *Reyelts* decision directly supporting the Keys' claim and strongly suggesting that class relief is appropriate. On Wednesday, the Fifth Circuit issued its decision in *Wendt v. 24 Hour Fitness USA, Inc*., __ F.3d __, No. 15-10309, at *5 n.14 (5th Cir. Apr. 13, 2016). The specific issue in that matter was whether customers of a fitness chain were

entitled to the return of all amounts paid based on an argument that the contracts were void under the Texas Health Spa Act. In holding that the customers were not entitled to relief, the Fifth Circuit specifically cited its decision in *Reyelts* and Section 4102.207(b) as a situation where such relief would be proper. The Fifth Circuit held that "Texas case law permits a plaintiff to recover the purchase price he paid under a void contract . . . if the statute that renders the contract void explicitly provides that the plaintiff is not liable to pay for any past services rendered by the defendant." To be clear, the Fifth Circuit *specifically cited* its decision in *Reyelts* and Section 4102.207(b) as a situation where Texas law permits a plaintiff to recover the purchase price it paid under a void contract.

Consistent with this decision, when considering Rule 42(b)(3) the single "question[] affecting only individual members" is the amount each individual homeowner paid to Lon Smith under the illegal contract. All other questions of law or fact are common to all class members. Accordingly, this situation is appropriate for class adjudication. [4]

Finally, class relief in this situation is necessary to protect Texas homeowners. It is critical to remember that contractors engaged in the unlicensed practice of public insurance adjusting prey upon the most vulnerable populations. *See* Bulletin #B-

[4] NAPIA agrees with the Keys that this case satisfies the other requirements of Rule 42.

0017-12. Such individuals are less likely to know their rights or to feel comfortable seeking legal help. Particularly following a catastrophic event like a hail storm, insured homeowners seeking to rebuild or repair the resulting damage can be quite vulnerable.[5] Victims of such catastrophes often are looking for help from anyone willing to offer it and are unlikely to check the offering party's training or qualifications. It is unfortunately increasingly common for unscrupulous contractors to target these victims in their weakened state by advertising themselves as "insurance claim specialists" and offering to "negotiate with your insurance company" to obtain the highest insurance payment possible in performing the necessary repairs. The inherent conflict of interest in allowing an unlicensed and unregulated contractor performing the roof repair work to also negotiate the final price that the insurance company will pay is insidious and inescapable.

Texans such as the Reyelts and the Keys work hard to pay their mortgages and their insurance premiums. As the facts of these matters illustrate, unlicensed

[5] Texas has recently experienced several significant catastrophic weather events, including a tornado and several hailstorms. Numerous recent news reports raises the problems with unlicensed and unregulated contractors taking advantage of Texas homeowners. *See, e.g.*, Jenny Suniga, *Beware of Scam Contractors During Cleanup*, KENS, Apr. 16, 2016, http://goo.gl/ZQ04j7; Haley Rogers, *Plano, Be Aware of Roof Scammers*, PLANO STAR COURIER, Mar. 30, 2016, http://goo.gl/0BiK10; Blair Ledet, *Shelby County Assessing Storm Damages: Officials Warn Against 'Fly-By-Night' Contractors*, KTRE, Mar. 29, 2016, http://goo.gl/uwP0nX; Jane Larson, *Houston Homeowner Loses $10K to Unlicensed Contractors*, KPRC, Mar. 21, 2016, http://goo.gl/L31iP0; Dave Lieber, *Watchdog: In Tornado's Wake, Protect Yourself From Bad Builders' Scams*, DALLAS MORNING NEWS, Dec. 27, 2015, http://goo.gl/LyCfxT; Domingo Ramirez, *Fort Worth Couple Pleads Guilty to Roofing Scam*, FT. WORTH STAR TELEGRAM, June 24, 2014, http://goo.gl/ZG0ZdG.

public insurance adjusting outside of the regulatory system set up to protect homeowners and ensure ethical conduct in the claims process results cannot be allowed to occur unchecked. A class action is the only feasible way of protecting and compensating the individuals most in need of protection and compensation.

The record in this case reflects a genuine urgency in comprehensive relief against Lon Smith in particular. The Keys have introduced a transcript of a telephone conversation in which Lon Smith offered a "reversed" high/low agreement, where Lon Smith would pay them $200,000 if it won summary judgment on the legality of the contract (including the collateral estoppel effect of *Reyelts*) and a mere $1,000 if the Keys won. 2 CR 676.[6] The intent of such a nefarious proposal is clear. Imagine if, faced with a sea of individual complaints, Lon Smith could find a homeowner willing to accept such an arrangement, so that it had a financial incentive to create good law for Lon Smith. The Court should affirm the certification order to protect against Lon Smith's attempts to divide its victims against themselves.

Texas homeowners deserve protection from contractors such as Lon Smith engaged in the unauthorized practice of public insurance adjusting. Such conduct is illegal under clear Texas law. Unfortunately, the conduct continues unabated across

[6] Lon Smith does not dispute the accuracy of the transcript. Rather, on the final page of its reply brief, it incorrectly says that the settlement offer is irrelevant and out-of-context.

Texas.[7] Certification of a class action against Lon Smith is appropriate and will send a strong message to all Texas contractors that such conduct must come to an end.

Prayer

For the foregoing reasons, NAPIA and TAPIA urge the Court to affirm the order certifying the class against Lon Smith.

Respectfully submitted:

/s/ *Steven J. Badger*
Steven J. Badger
State Bar No. 01499050
sbadger@zelle.com
ZELLE LLP
901 Main Street, Suite 4000
Dallas, Texas 75202
(214) 742-3000

Of counsel:

Brian S. Goodman
bgoodman@kg-law.com
Steven M. Klepper
sklepper@kg-law.com
KRAMON & GRAHAM, P.A.
One South Street, Suite 2600
Baltimore, Maryland 21202-3201
(410) 752-6030

Counsel for Amici Curiae

[7] A simple Google search of the phrase "Texas roof contractor insurance claim specialist" illustrates the severity of the problem, as countless roofing contractor websites are listed offering such illegal services.

Certificate of Compliance

1. This brief complies with the type-volume limitations of Texas Rule of Appellate Procedure 9.4(i)(2)(B) because it contains 3,450 words, excluding the parts of the brief exempted by Texas Rule of Appellate Procedure 9.4(i)(1).

2. This brief complies with the typeface requirements of Texas Rule of Procedure 9.4(e) because this brief has been prepared in a proportionally spaced typeface using Microsoft Word 2010 in fourteen point Times New Roman font.

/s/ *Steven J. Badger*
Steven J. Badger

Certificate of Service

I hereby certify that a true and correct copy of the foregoing document was forwarded via electronic filing on April 18, 2016, to the following counsel of record:

Robert C. Wiegand
bob.wiegand@swolegal.com
STEWART WIEGAND & OWENS PC
325 North St. Paul Street
Suite 4150
Dallas, Texas 75201
Counsel for Appellants

Shawn M. McCaskill
smccaskill@godwinlaw.com
GODWIN PC
1201 Elm Street, Suite 1700
Dallas, Texas 75270
Counsel for Appellants

Rick K. Disney
rdisney@csa-lawfirm.com
COTTEN SCHMIDT & ABBOTT, LLP
550 Bailey Ave., Suite 600
Fort Worth, Texas 76107
Counsel for Appellants

H. Dustin Fillmore, III
dusty@fillmorefirm.com
Charles W. Fillmore
chad@fillmorefirm.com
THE FILLMORE LAW FIRM, L.L.P.
901 Lake Street
Fort Worth, Texas 76102
Counsel for Appellees

Marshall M. Searcy, Jr.
marshall.searcy@kellyhart.com
Bill Warren
bill.warren@kellyhart.com
Matthew D. Stayton
matt.stayton@kellyhart.com
David H. Garza
david.garza@kellyhart.com
KELLY HART & HALLMAN LLP
201 Main Street, Suite 2500
Fort Worth, Texas 76102
Counsel for Appellees

/s/ *Steven J. Badger*
Steven J. Badger