

Diminution In Value And Commercial Insurance In Ga.

Law360, New York (January 10, 2011) -- When nearby construction work allegedly caused an office building's floor tiles to crack, the building owner, Royal Capital Development LLC, sought to recover its losses under a commercial insurance policy covering the building. Royal Capital sought not only the costs to repair the physical damage, but also the diminution in value the property purportedly sustained because of the "stigma associated with the damage caused by the incident." Royal Capital Dev. LLC v. Md. Cas. Co., No. 1:10-CV-1275-RLV, 2010 U.S. Dist. LEXIS 133911, at *3 (N.D. Ga. Dec. 2, 2010).

Assuming, without deciding, that the property suffered diminution in value, Judge Robert L. Vining Jr. of the U.S. District Court for the Northern District of Georgia held that diminution in value was not recoverable under the policy, in his December 2010 order granting the insurance company's motion for summary judgment. Judge Vining's decision appears to render ineffectual a controversial directive issued by the Georgia commissioner of insurance, John W. Oxendine, in April 2010 (Directive 10-EX-1).

This article will outline the lead Georgia Supreme Court decision on which Royal Capital and Oxendine relied for their position that diminution in value was insured under a commercial property insurance policy, as well as Judge Vining's reasoning rejecting that position.

Diminution in value is recoverable under automobile insurance policies in Georgia.

The Supreme Court of Georgia held that insurance companies are liable to compensate policyholders for diminution in the value of their vehicles after automobile accidents. State Farm Mut. Auto. Ins. Co. v. Mabry, 274 Ga. 498, 509 (2001). In Mabry, the vehicle owners claimed diminution in value losses due to physical damage their vehicles had sustained. Id. at 498. The policies provided that the insurance company would "pay for the loss to your car." Id. at 502. The policies allowed the insurance company to choose between paying the actual cash value of the car or paying to "repair or replace the property or part with like kind and quality." Id.

The vehicle owners argued the policies obligated the insurance company to consider the diminution in value a vehicle suffers by virtue of being involved in an accident when assessing the loss. *Id.* On the other hand, the insurance company maintained that when it chose to pay the cost to “repair or replace the property,” it was not liable for any diminution in value to the vehicle because repair returns a vehicle to its “pre-loss condition in terms of appearance and function.” *Id.* at 502-03. The court surveyed a long line of Georgia cases and reached the following conclusion:

"The foregoing review of Georgia case law establishes clearly that value, not condition, is the baseline for the measure of damages in a claim under an automobile insurance policy in which the insurer undertakes to pay for the insured's loss from a covered event, and that a limitation of liability provision affording the insurer an option to repair serves only to abate, not eliminate, the insurer's liability for the difference between pre-loss value and post-loss value." *Id.* at 506.

The Mabry decision can reasonably be understood to allow recovery for diminution in value under an automobile insurance policy that covers physical damage, even if the insurance company elects to pay for repairs that restore the vehicle to its “pre-loss condition in terms of appearance and function,” if the court finds that the vehicle has less than its pre-loss value even after repairs. The court noted that Georgia holds the minority view.

A directive by the Georgia commissioner of insurance applied the Georgia Supreme Court's reasoning allowing diminution in value coverage under automobile insurance to commercial insurance policies.

In April 2010, while Royal Capital was pending, Georgia Commissioner of Insurance John W. Oxendine issued a controversial directive in which he stated that diminution in value could be recoverable under commercial insurance policies. Specifically, the commissioner addressed whether the Mabry court's holding that “physical damage resulting from a covered event can reduce the value of a vehicle, and insurers should assess diminution of value along with the elements of physical damage when a policyholder makes a general claim of loss” applies to commercial real property claims. The commissioner opined that it does in the absence of “specific policy language to the contrary.” In reaching this conclusion, the commissioner noted that “this issue has not been addressed either by the legislature or the courts of this state.” Directive 10-EX-1.

This directive engendered some political debate as Royal Capital's owner and his associates reportedly gave \$46,000 to Oxendine's 2010 campaign for governor. On July 16, 2010, the Atlanta Journal Constitution stated, “The directive does not mention Royal Capital by name, but it clearly takes its side in the issue.”

The recent ruling holding that diminution in value is not recoverable under the commercial insurance policy at issue.

Despite Directive 10-EX-1, Judge Vining held that diminution in value was not recoverable under Royal Capital's commercial insurance policy. *Royal Capital Dev.*, 2010 U.S. Dist. LEXIS 133911, at *7. Royal Capital cited the Supreme Court decision of *Mabry* and the unpublished Northern District Court decision of *Nuco Investments Inc. v. Hartford Fire Insurance Co.*, No. 1:02-CV-1622-CAP, 2005 U.S. Dist. LEXIS 33350 (N.D. Ga. Dec. 5, 2005) in support of its motion for summary judgment, but Judge Vining refused to follow those cases.

The court found *Mabry* was inapplicable because it "dealt exclusively with a consumer automobile policy," and the court distinguished *Nuco* on the ground that the policy at issue there "contained a very different 'Loss Payment' clause." *Royal Capital Dev.*, 2010 U.S. Dist. LEXIS 133911, at *7-8 n.3. Noting that "this matter boils down to simple policy interpretation," the court based its decision on an interpretation of the two policy provisions at issue: the coverage grant and the payment option provision. *Id.* at *6.

Regarding the coverage grant, the court noted that the only Georgia case to interpret the policy language, "direct physical loss of or damage to covered property," — *AFLAC Inc. v. Chubb & Sons Inc.*, 260 Ga. App. 306 (2003) — held that the provision did not cover economic losses. The court explained that while AFLAC did not specifically address diminution in value, "the Court of Appeals of Georgia in that case was clear that the parties to an insurance policy could limit damages by the terms of the insurance policy." *Id.* at *7 n.2.

Regarding the payment option provision, the court noted that the policy allowed the insurance company to choose one of four "distinct and mutually exclusive" options, and the insurance company elected to "[p]ay the cost of repairing or replacing the lost or damaged property." *Id.* at *6. Other payment options included:

- Pay the value of lost or damaged property.
- Take all or any part of the property at an agreed or appraised value.
- Repair, rebuild or replace the property with other property of comparable kind and quality.

The court held, "Because the parties limited the defendant's liability by the terms of their policy and because a plain reading of the policy shows that 'diminution of value damages' are not meant to be included in the option selected by the defendant, the defendant is entitled to summary judgment." *Id.* at *7.

Thus, the order leaves open the possibility that diminution in value damages may be recoverable under another option of the payment option provision. It is still not entirely clear how Georgia state courts will rule on the question of whether diminution in value is recoverable under commercial insurance policies. According to the *Royal Capital* decision, however, policyholders' claims for diminution in value are substantially weaker in commercial property cases than Directive 10-EX-1 would suggest.

--By Jane Warring and Taylor Davis, Robins Kaplan Miller & Ciresi LLP

Jane Warring (jewarring@rkmc.com) and Taylor Davis (tldavis@rkmc.com) are associates in the Atlanta office of Robins Kaplan Miller & Ciresi LLP in the firm's insurance department.

The opinions expressed are those of the authors and do not necessarily reflect the views of the firm, its clients, or Portfolio Media, publisher of Law360.

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