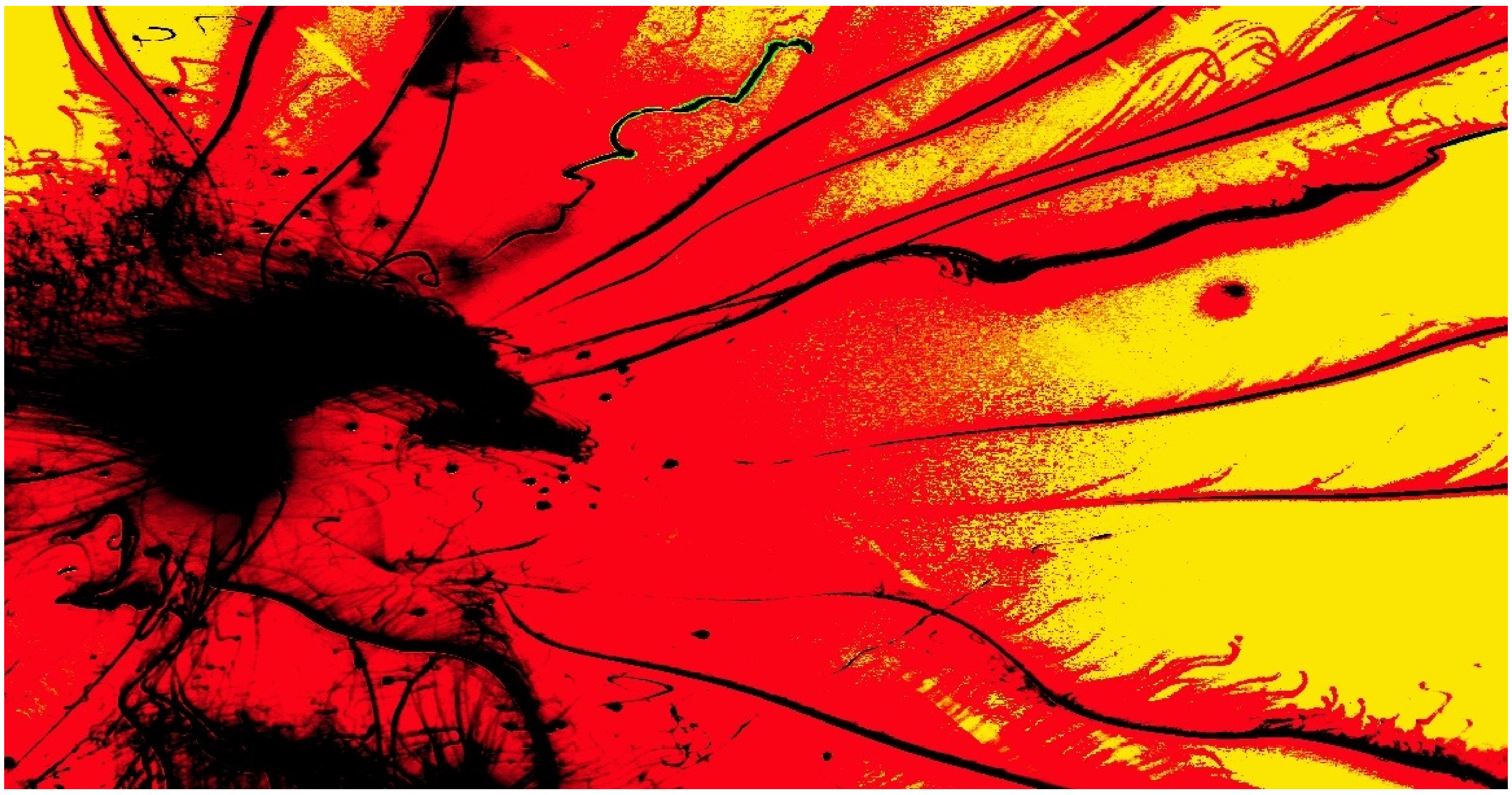


CARR MALONEY PC

ASSESSING TOTAL LOSS DAMAGE: THE IMPLICATIONS OF THE BROAD EVIDENCE RULE

By Aleksandra Rybicki, Esq.

When an insured property owner suffers a total loss, insurance adjusters frequently find themselves embroiled in settlement negotiations and attempt to limit the company's payout by closely assessing damages. While this assessment plays an important role at the pre-lawsuit settlement stage, it warrants strategic advocacy at the litigation stage.

Consider the following scenario. Twenty years ago, Walter Windfall bought a building for $1 million to start his law firm. One day, the building, which Walter had insured, burns to the ground. Like many insurance policies, Walter's policy allows recovery of the actual cash value (ACV) of his property but does not define ACV. Walter's appraiser says that replacing the building will cost $3 million.

Under the Fair Market Value Rule, currently used in 11 states,[1] Walter would be entitled to the difference between the fair market value of the property before and after the loss. Since the property was destroyed entirely, applying the Fair Market Value Rule would overcompensate Walter because he would be gaining an entirely new building with a much longer useful life.

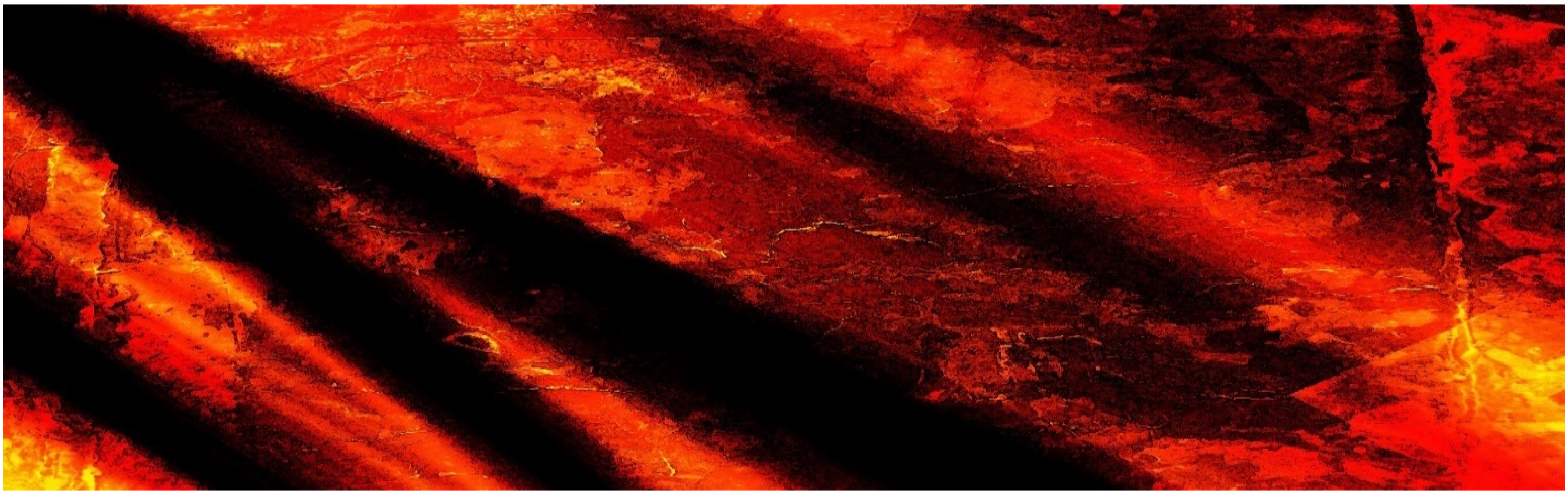
In contrast, under the Replacement Cost Minus Depreciation Rule, used in 4 states,[2] the replacement cost is reduced by the loss in the property's residual value. Thus, if at the end of its 50-year useful life, the building would have had a residual value of $200,000, the building's depreciation – the cost of the building minus the residual value ($1 million - $200,000) – would be $800,000. Applying the Replacement Cost Minus Depreciation Rule ($3 million - $800,000), it would cost Walter's insurance company $2.2 million to make Walter whole.

While this approach seems sound because Walter is not getting an entirely new building, there are circumstances under which this method would be unfair. If, for example, at the time of the fire, Walter's building was obsolete – that is, if it had very little value to Walter for purposes of either use or sale – $2.2 million would overcompensate Walter. When applying both calculations, it is possible for the insured to end up in a better position after the loss than before the loss and, thus, provides insureds with an incentive to cause a loss. **(continued on next page)**

Aleksandra Rybicki is a litigation attorney who focuses her practice on complex litigation and liability matters, including general, professional and product liability.

Aleksandra graduated from the George Washington University School of Law, where she was Editor of the American Intellectual Property Law Association Journal. While attending law school, she was a Judicial Intern for both the Honorable Wendell P. Gardner, Jr., Associate Judge for the Superior Court of the District of Columbia, and the Honorable Kiyo A. Matsumoto, United States District Court Judge for the Eastern District of New York.

Prior to joining Carr Maloney, Aleksandra was a Law Clerk for the Honorable Sean D. Wallace, Associate Judge in the Circuit Court for Prince George's County, Maryland.



THE IMPLICATIONS OF THE BROAD EVIDENCE RULE

(continued from previous page)

Approximately 20 states[3] have addressed these issues by adopting the Broad Evidence Rule. The Broad Evidence Rule originated in the seminal case *McAnarney v. Newark Fire Ins. Co.*, 159 N.E. 902 (N.Y. 1928) (explained in *SR Int'l Bus. Ins. Co. v. World Trade Center Props., LLC*, 445 F. Supp. 2d 320, 342-45 (S.D.N.Y. 2006)), where the Court held that all factors that bear on the value of the property should be considered when determining the payment that would restore the insured to the status quo ante. Such factors include market value, replacement cost, depreciation, original cost, condition of the property, location, use, assessed value and offers to sell. The Broad Evidence Rule is an inclusive valuation method that allows any evidence that can establish correct property value. Specifically, the Rule allows an accurate determination of the loss incurred without overcompensating insureds. Although many courts have used the Rule since then, courts refrain from referring to admission of more expansive evidence as doing so under "the Broad Evidence Rule." Additionally, courts have not specifically enumerated the factors to be considered under the Rule, or what weight should be given to each factor.

Both Maryland and Virginia have adopted the Broad Evidence Rule, while the District of Columbia and West Virginia remain undecided. The Maryland Court of Appeals held that the determination of "cost of production less depreciation" was not the only factor in ACV analysis. Rather, it was merely one among other sources of evidence. *Schreiber v. Pacific Coast Fire Ins. Co.*, 75 A.2d 108, 111 (Md. 1950). Since then, Maryland courts have routinely considered several factors contributing to the determination of damages. For example, in *Fred Frederick Motors, Inc. v. Krause*, 12 Md. App. 62 (Md. 1971), the Court of Special Appeals rejected the determination that a car dealer's recovery was limited to the cost of repairs of the damaged cars and held that "if a plaintiff can prove that after repairs his vehicle has a diminished market value from being injured, then he can recover in addition to the cost of repairs the diminution in market value, provided the two together do not exceed the diminution in value prior to the repairs."

Likewise, Virginia adopted the Broad Evidence Rule in 1961, when in an action to recover under an insurance policy for windstorm damage to property, the court held that replacement or reproduction costs, less depreciation, was an important factor in determining ACV. *Harper v. Penn Mut. Fire Ins. Co.*, 199 F. Supp. 663, 665 (E.D. Va. 1961) (applying Virginia law). The Court reasoned that "strict adherence to either of the recognized tests of 'market value' or 'reproduction cost less depreciation' will merely serve to shackle the trier of fact in all cases."

Given the state of the law, insurers should define ACV in their policies by incorporating factors courts have considered under the Broad Evidence Rule. This approach prevents overcompensation and provides adjusters and their attorneys bargaining power at both the settlement and litigation stages. If a policy lacks an ACV definition, attorneys practicing in Broad Evidence Rule jurisdictions, like Maryland and Virginia, should seek admission of relevant evidence to accurately determine damages. Attorneys in undecided jurisdictions should cite to neighboring jurisdictions and advocate for the Rule's adoption.

1) Alabama, California, Delaware, Georgia, Maine, Missouri, Nebraska, New Mexico, North Dakota, Texas, and Washington.
2) Illinois, Louisiana, Ohio, Oregon.
3) Colorado, Connecticut, Florida, Idaho, Indiana, Iowa, Kentucky, Maryland, Massachusetts, Michigan, Minnesota, Montana, New Hampshire, New Jersey, New York, North Carolina, Oklahoma, Rhode Island, South Carolina, South Dakota, Vermont, Virginia, Wisconsin.