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Appraisal Award Cannot Trump Policy Terms Delineating The Scope Of Coverage.

By Amanda B. Fopma & Drew W. Broaddus

Property insurers are becoming all too familiar with disputes over the Actual Cash Value (“ACV”) and Replacement Cost Value (“RCV”). Insureds often purchase policies or endorsements allowing for the limit of liability to be adjusted to accommodate full replacement of the damaged property, whether the damaged property is a dwelling, other structure, or contents. With increasing regularity, there is a disagreement following a loss between the insurer and the insured over the amount recoverable under these provisions. Appraisal provides an avenue to resolve the dispute as to the ACV, short of litigation, that can be invoked by either party. Under the appraisal process established by MCL 500.2833(1)(m), each party selects their own appraiser and, if the appraisers cannot agree as to the amount of loss within a reasonable period of time, the appraisers submit their differences to an umpire. A written appraisal award sets the amount of loss when it is signed by the umpire and either of the appraisers. The process is intended to be “a substitute for judicial determination of a dispute concerning the amount of loss.”¹ Therefore, judicial review of an appraisal award that is conclusive as to the amount of loss is “limited to instances of bad faith, fraud, misconduct, or manifest mistake.”² However, the appraiser cannot decide questions about insurance *coverage*, and if he or she does so, the decision is subject to judicial review.³

SECRET WARDLE NOTES:

One of the key considerations for the Court was whether the appraisal award entitled the insured only to the ACV versus RCV. If the appraisal award is drafted in such a way that it can be regarded as conclusively establishing the insured’s entitlement to RCV, a court would probably only be able to review it in cases of bad faith, fraud, misconduct, or manifest mistake.

It will serve insurers well if the appraisal award can be drafted in such a way as to clearly articulate the amount (ACV v RCV) the insured is entitled to. Beyond that, simply including language that the appraisal award remains “subject to all of the policies terms and conditions” may foreclose these type of disputes later on.

While the appraisal award should settle most disputes, it doesn’t always. One situation where problems arise, even after an appraiser has resolved the valuation issues, is when the insured decides to actually replace the dwelling, other structures, and/or contents under the replacement provisions of the Policy. Many policies state that the insurer will pay no more than ACV *until actual repair or replacement is completed*. Beyond that, ACV is generally defined as including a deduction for depreciation.⁴ As a result, most appraisal awards specifically set forth the Replacement Cost, Applicable Depreciation and ACV. Increasingly, however, insureds are arguing that when the appraisal award sets RCV, this relieves the insured of their obligation under the policy terms to provide proof of actual replacement and cost.

The insured made such an argument in *Dupree v Auto-Owners*, __ Mich __ (2014) (No. 147647), a case in which the Supreme Court recently clarified when an insured had a continuing obligation to submit proof of actual replacement under the policy following an appraisal award. In *Dupree* the insured suffered a fire loss resulting in extensive damage to the dwelling and her contents. She sought coverage under her homeowner’s policy, which provided for replacement cost benefits. The parties resolved the dwelling portion of the claim, but were unable to reach an agreement as to the value of the lost contents. An umpire issued an appraisal award which read: “(1) THE FULL COST

¹*Auto-Owners v Kwaiser*, 190 Mich App 482, 486 (1991).

²*Kwaiser*, 190 Mich App at 486.

³*Kwaiser*, 190 Mich App at 487; MCL 500.2833(1)(m).

⁴Such provisions – which limit the insurer’s liability to amounts specified in the policy, unless the damage property is actually repaired, rebuilt and/or replaced – are specifically authorized by MCL 500.2826.

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OF REPAIR OR REPLACEMENT IS \$167,923.60; (2) APPLICABLE DEPRECIATION.... \$39,673.48; (3) THE ACTUAL CASH VALUE LOSS IS.... \$128,250.12.” *Dupree*, Slip Op at 2-3.

Following the appraisal, Auto-Owners issued a settlement draft to Dupree in the amount of \$128,250.12. Although the policy provided for RCV, Auto-Owners believed it only requires to pay the ACV because Dupree had failed to comply with the policy’s RCV provision. That provision established *actual replacement of the property* as a condition precedent to payment of the recoverable depreciation. The trial court disagreed with Auto-Owners and granted Dupree’s motion for summary disposition. The Court of Appeals affirmed. Auto-Owners filed an application for leave to appeal to the Michigan Supreme Court. The Supreme Court, “lieu of granting [Auto-Owners’] application for leave to appeal,” reversed “the judgment of the Court of Appeals and remand[ed]” to the trial court “for entry of an order vacating its ruling in plaintiff’s favor and granting summary disposition in favor of” Auto-Owners. *Dupree*, Slip Op at 5-6.

Focusing on the language of the appraisal award stating “We...do hereby award as the Actual Cash Value of said property” the Court held the only portion of the appraisal award which constituted a conclusive judgment under the MCL 500.2833(1)(m) was the ACV award. Mindful of the limited circumstance in which judicial review of an appraisal award is available, the Court held:

...[The] deference [ordinarily shown to the appraisal award] is inapplicable because the issue here pertains to a condition *precedent* that has not been met under the terms of the insurance policy, namely, submission of proof of actual loss. Accordingly, before it can be determined that the appraisal award constituted a conclusive judgment for replacement cost that superseded the insurance policy’s replacement cost provisions, there is the preliminary question concerning whether the appraisal award entitled plaintiff to the replacement cost or the actual cash value of her damaged personal property.

Because the appraisal award cannot be read as a “conclusive” judgment for replacement cost, the terms of the replacement cost provision under the insurance policy control the scope of plaintiff’s appraisal award. Consequently, plaintiff’s failure to submit proof of actual loss in accordance with that provision entitles her to only the [ACV].... *Dupree*, Slip Op at 5.

CONTACT US

Troy
2600 Troy Center Drive, P.O. Box 5025
Troy, MI 48007-5025
Tel: 248-851-9500 Fax: 248-851-2158

Lansing
6639 Centurion Drive, Ste. 100, Lansing, MI 48917
Tel: 517-886-1224 Fax: 517-886-9284

Grand Rapids
2025 East Beltline SE, Ste. 600, Grand Rapids, MI 49546
Tel: 616-285-0143 Fax: 616-285-0145

www.secrestwardle.com

CONTRIBUTORS

Insurance Coverage Practice Group Chair
Mark E. Morley

Editor
Linda Willemsen

We welcome your questions and comments.

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