2007 Insurance Coverage Update – Focus on First-Party Coverage Issues

THE BROAD EVIDENCE RULE

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Introduction

The "broad evidence rule" supplies a methodology for determining the value of damaged property in first party property insurance cases where property is insured for "actual cash value" and that term is not otherwise defined in the policy. The rule is that when determining the amount of insurance proceeds to compensate an insured for its damaged or destroyed property, the finder of fact (i.e., the judge, jury, or appraiser) must consider **all** relevant evidence that might help to determine the value of that property. A finder of fact who excludes any evidence relevant to the valuation of that property commits reversible error. The rule favors the broadest consideration of all relevant evidence pertaining to the value of the damaged or destroyed property, which accounts for its name, "the broad evidence rule".

The New York State Court of Appeals adopted the rule in 1928. Since that time, it has been clarified and refined in numerous cases to accomplish its goal of indemnification of the insured, which is fact specific to the various special circumstances at issue. The factual scenario in which the rule was first articulated was unique and provided an ideal background to expound upon concepts of valuation and indemnity.

Origins and Purpose of the Broad Evidence Rule

The "broad evidence rule" was first introduced by the New York State Court of Appeals in 1928 in the case of *McAnarney v. Newark Fire Insurance Company of New York*, 247 N.Y. 176, 159 N.E. 902 (1928). The difficulty in making a valuation of property in *McAnarney* was that it involved property that no longer served a useful purpose.

In1919, the plaintiff in *McAnarney* purchased real estate upon which stood seven buildings designed for the manufacture of malt alcohol. The purchase price was $8000. Due to the passage of the National Prohibition Act in 1918, the manufacture of alcohol was prohibited and since that time the buildings were not employed for any useful purpose.

In January 1920 the plaintiff purchased fire insurance policies covering the property. In April of the same year, the buildings were destroyed by fire. The plaintiff submitted a proof of loss to its insurance companies wherein he valued the buildings at $60,000. The defendant, Newark Fire Insurance Company, which was one of several insuring companies, refused to issue payment of its $2,500 policy limits. The action was tried before a jury, which returned a verdict in the amount of $55,000 for the value of the buildings.

On appeal, the defendant contended that the trial court erred in refusing to admit the following evidence pertaining to the valuation of the property: (a) the plaintiff, who had been a director of the brewing company that operated the brewery located within the subject buildings, had been unable to obtain a purchaser for the property; (b) the plaintiff advertised the property for sale for the sum of $12,000; (c) the plaintiff submitted an affidavit to the local board of assessors in which he stated that the property had no value except for the production of malt and that the production of malt upon the premises had entirely ceased, (d) that the owners would have accepted $15,000 for the property, and (e) that the best offer that the owners had received for the property was $6,000.

Additionally, the defendant contended on appeal that the trial court erred when it charged the jury as follows: (a) "Your answer shall not be the market value – shall not be the sum that the buildings would sell for, but what it cost to build them – what it cost to build the structures, less depreciation proven in the case;" (b) it is immaterial that the passage of the National Prohibition Act caused the buildings to no longer be employed for any useful purpose; and (c) the value of the buildings destroyed was to be measured solely by the cost of replacement less deductions for depreciation.

On appeal, the Court of Appeals held that the trial court had committed reversible error by excluding the foregoing evidence and by charging the jury in the manner set forth above. Thus, the Court of Appeals reversed and ordered a new trial. In reaching that determination, the Court of Appeals considered the language of the insurance policy and the law of damages.

The insurance policy in *McAnarney* contained the following provision:

> The insurance company does insure . . . to the extent of the actual cash value (ascertained with proper deductions for depreciation) of the property at the time of loss or damage, but not exceeding the amount which it would cost to repair or replace the same with material of like kind and quality within a reasonable time after such loss or damage.

The *McAnarney* court held that it disagreed with the defendant insurer, which contended that actual cash value is the same as market value. It also disagreed with the plaintiff insured who contended that actual cash value is merely the replacement cost less depreciation

The Court held that the term "actual cash value" it is much broader than "market value" and that market value as an exclusive measure of damages does not apply. The court reasoned that, if market value were the rule, property for which there is no market

would possess no insurable value. The court stated that this proposition "is clearly untenable." *McAnarney*, 247 N.Y. at 180.

The *McAnarney* court stated that, to ascertain "actual cash value", one must look beyond the terms of the insurance policy and to the general principles of the law of damages. The court held as follows:

> Indemnity is the basis and foundation of all insurance law. [Citations omitted.] The contract of the insurer is not that, if the property is burned, he will pay its market value, but that he will indemnify the assured, that is, save him harmless or put him in as good a condition, so far as practicable, as he would have been in if no fire had occurred. . . Where insured buildings have been destroyed, the trier of fact may, and should, call to its aid, in order to effectuate complete indemnity, every fact and circumstance which would logically tend to the formation of a correct estimate of the loss. It may consider original cost and cost of reproduction; the opinions upon value given by qualified witnesses; the declarations against interest which may have been made by the assured; the gainful uses to which the buildings might have been put; as well as any other fact reasonably tending to throw light upon the subject.

McAnarney, 247 N.Y. at 184.

The Court of Appeals found it highly relevant in *McAnarney* that the buildings at issue became obsolete due to the passage of the National Prohibition Act. This is because the insurance policy required the trier of fact to make proper "deductions for depreciation". The court held that:

> In the case at bar the trier of fact, in considering cost of reproduction, was required by the policy to make proper 'deductions for depreciation.' 'The word (depreciation) means, by derivation and common usage, a 'fall in value; reduction of worth." N. Y. Life Ins. Co. v. Anderson (C. C. A.) 263 F. at p. 529. It includes obsolescence. Nashville, C. & St. L. R. Co. v. United States (C. C. A.) 269 F. 351, at p. 355; San Francisco & P. S. S. Co. v. Scott (d. c.) 253 F. 855. An obsolete thing is a thing no longer in use. In determining the extent to which these buildings had suffered from depreciation, the trier of fact should have been permitted to consider that, owing to the passage of the National Prohibition Act, they were no longer useful for the purposes to serve which they were erected.

> It should have been permitted to consider their adaptability or inadaptability to other commercial purposes.

McAnarney, 247 N.Y. at 185.

To the same effect: *Sebring v. The Firemen's Ins. Co. of Newark*, 107 A.D. 2d. 902, 483 N.Y.S. 849 (4th Dept. 1929) (It was reversible error to exclude other evidence of value and limit the actual cash value to replacement cost less depreciation. Likewise, it was reversible error to charge the jury that the measure of damages was replacement cost less depreciation.)

Following *MCAnarney,* the Court set aside an appraisal award in *Gervant v. New England Fire Ins.*, 306 N.Y. 393, 118 N.E. 2d 574 (1954) because the insurer's appraiser and the court appointed umpire only considered replacement cost less depreciation in determining the value of a commercial building in Brooklyn. The building was covered for loss and damage by fire and was partially destroyed by fire. When the insured and insurer could not agree on the amount of loss and damage the parties commenced an appraisal proceeding. The insured sued to set aside the appraisal award because the insurer's appraiser and the umpire refused to consider other relevant factors in determining the value. The appraisal award did not take into consideration the age, original cost of construction, market value prior the fire, or the rental income of the building that was brought to their attention by the insured's appraiser. The Court held that reliance solely upon replacement cost less depreciation in establishing an appraisal award was such misconduct as to set aside the award:

> Here the umpire and the company's appraiser arbitrarily refused to admit evidence of the variety of facts which enter into the determination of 'actual cash value' despite the fact that evidence of such factors was

> directly presented to them by plaintiff's appraiser. They flatly refused to take any evidence into account other than that relating to reproduction cost less depreciation. This does not present a situation, as defendant contends, where the Appellate Division has undertaken to review the merits of the appraisal. It is manifest that the Appellate Division based its determination on the rule that an umpire and one appraiser are not on the rule that an umpire and one appraiser are free to disregard, arbitrarily, pertinent evidence presented by the other appraiser, and that a flat refusal on their part to hear such evidence is condemned by authorities in this State as legal misconduct for which the award will be set aside.

Gervant, 306 N.Y. at 399.

To the same effect: *Sebring v. The Firemen's Ins. Co. of Newark*, 107 A.D. 2d. 902, 483 N.Y.S. 849 (4th Dept. 1929) (It was reversible error to exclude other evidence of value and limit the actual cash value to replacement cost less depreciation. Likewise, it was reversible error to charge the jury that the measure of damages was replacement cost less depreciation.)

In *Cass v. Finger Lakes Co-op Ins. Co.*, 107 A.D. 2d 904, 483 N.Y.S.2d 849 (3rd Dept. 1985) the insurer claimed that the plaintiff's proof was insufficient to establish actual cash value of the fire damage. The court, applying the broad evidence rule, held for the insured and sustained the jury's verdict, which was supported by "detailed evidence of the repair and replacement cost for the building...testimony of a qualified real estate broker as to the market value of the building before and after the fire...photographs of the fire damage, verbal descriptions of the building's condition, age and purchase price ..."

Cass, 107 A.D. 2d at 905.

The "broad evidence rule" was not applied in *SR International Business Insurance Company, Ltd. v. World Trade Center Properties, LLC*, 445 F. Supp.2d 320

(2006) because the policy specifically defined actual cash value to be more restrictive than the valuation clause in the *McAnarney* policy. In *SR International*, the insurance policy provided as follows:

> "Actual Cash Value" means the cost to repair, rebuild or replace the lost or damaged property, at the time and place of the loss, with other property of comparable size, material and quality, **less allowance for physical deterioration, depreciation, obsolescence and depletion**. (Emphasis added.)

SR International, 445 F. Supp.2d at 341-342.

In *SR International*, the insurers argued that the above definition of "actual cash value" required the appraisers to consider all pertinent evidence, including market value and the factors that a real estate appraiser would normally consider in evaluating market value, including depreciation of property, and evidence of both economic and functional obsolescence, as well as physical deterioration. In other words, the insurers sought application of the "broad evidence rule" in determining the "actual cash value". The plaintiffs argued that "actual cash value" should be determined in accordance with the plain meaning of its definition in the policy.

The District Court, in refusing to apply the broad evidence rule held:

> In view of the highly inclusive language courts have used to express the broad evidence rule ('all pertinent evidence," *Gervant*, 306 N.Y. at 398, 118 N.E.2d 574; "any ... fact reasonably tending to throw light on the subject," *Incardona*,60 A.D.2d at 750, 400 N.Y.S.2d at 945), I find it inconceivable that if the parties had sought to incorporate that rule into the Travelers form, they would not have used some facially inclusive language instead of listing only particular factors.

S.R.International at 445 F. Supp. 2d at 344.

Likewise, in *Bowles v. Travelers Indem. Co.*, 149 A.D. 2d 936, 540 N.Y.S.2d 69 (4th Dept. 1989), the insured suffered a loss by fire to his home covered by an all risk homeowners policy that covered the premises for "'actual cost to repair or replace that part of the building damaged' up to the applicable limit of liability." (at 937) The court held that the broad evidence rule did not apply to this policy and that it was error to dismiss the complaint at trial for plaintiff's failure to prove actual cash value.

Actual Cash Value Before the Loss Less Market Value After the Loss

There is some confusion as to whether the insured must prove the market value of the insured premises after a loss, particularly where there is a partial loss, to satisfy the requirements of the broad evidence rule. This uncertainty has been noted in the Comments to *Pattern Jury Instructions* for the damages charge in fire insurance cases: "Whether in partial loss cases the value after the fire is to be considered is not clear." 2 PJI 2d 4:49 at 871 (2007).

The requirement first appeared in *Molot, Inc. v. Commonwealth Insurance Company of New York*, 10 A.D.2d 683, 197 N.Y.S.2d 495 (1st Dept. 1960). *Molot* involved furs that were damaged in a fire. The insured disposed of the furs 15 months after the fire, at an auction. The insured presented evidence of the cost of the furs, the replacement cost and the amount it received upon selling them at auction after the fire. The First Department held that such proof was insufficient to establish damages pursuant to the broad evidence rule:

> [T]he award with respect to damages must be set aside because there was no proper proof of damage. The 'actual cash value' of the property at the time of the loss is the standard which must be used under the terms of the policy in order to determine the amount for which the defendants may

> be held liable. Replacement cost in and of itself is no proof of 'cash value'. Nor is the cost of the furs sufficient to establish the actual 'cash value' of the furs. In view of the fact that the merchandise damaged was retained and disposed of by the plaintiff, the amount for which the defendants may be held liable is **the difference between the 'actual cash value' of the property at the time just preceding the fire and the market value immediately after the fire**. We have no proof as to either of these items. The price obtained when the goods were sold at auction some 15 months after the fire does not represent the market value thereof immediately after the fire. *Molot, Inc.*, 10 A.D.2d at 683. [Emphasis added.]

Shortly after *Molot* was decided in the First Department, a first party damages dispute was litigated in the Second Department, *Eshan Realty Corp. v. Stuyvesant Insurance Company of New York*, 25 Misc.2d 828, 202 N.Y.S.2d 899 (Sup. Ct., Kings County 1960) (*modified*) 12 A.D.2d 818, 210 N.Y.S.2d 256 (2nd Dept. 1961) aff. 11 N.Y.2d 707, 181 N.E.2d, 218 (1962), with arguably a different holding. In *Eshan*, the insured suffered a partial fire damage to an old apartment building having cold water flats. The at the conclusion of a non-jury trial the court held that the insured could recover the lesser of the actual cash value of the building taking depreciation and all other evidence of value into consideration or the cost to repair or replace the property. After the fire, the insured sold the building for $12,000. The trial court would have reduced the cost to repair by this sum. However, the Second Department held that the proceeds of the sale after the loss were not material to the loss calculation. The Court of Appeals affirmed without decision. The decision provided no requirement that the insured must prove the market value after the loss to recover from its insurer. Indeed, *Gervant v. New England Fire Ins., supra* was a partial damage loss in which the Court of Appeals made no reference to the insured's obligation to prove the after loss market value of the damaged property.

However, *Molot* was relied upon in a later Fourth Department case, *Incardona v. Home Indemnity Company*, 60 A.D.2d 749, 400 N.Y.S.2d 944 (4th Dept. 1977), which dismissed the complaint because the plaintiff, who suffered a partial fire loss of real property, failed to submit sufficient evidence of "actual cash value". The plaintiff merely submitted evidence of the cost to repair the property, but failed to submit evidence of the cost of depreciation, and failed to submit any evidence of the market value after the loss to establish actual cash value. The court, citing *McAnarney*, held that:

> The purpose of an action on a fire insurance policy is to attempt to put the insured in as good a position as he would have been had no fire occurred, by awarding him the actual cash value of the property lost or damaged.. . While reproduction cost less depreciation is competent evidence of actual cash value in a fire loss (Kramnicz v. First Nat. Bank of Greene, 32 A.D.2d 1009, 1010, 302 N.Y.S.2d 22, 27), it is error to instruct the jury that reproduction cost less depreciation is the sole measure of actual cash value. The general rule in New York is that the trier of facts "may consider original cost and cost of reproduction; the opinions upon value given by qualified witnesses; the declarations against interest which may have been made by the assured; the gainful uses to which the buildings might have been put; as well as any other fact reasonably tending to throw light upon the subject" (McAnarney v. Newark Fire Ins. Co., 247 N.Y. 176, 184, 159 N.E. 902, 905; see, 31 N.Y. Jur. Insurance §1384 *et seq.; 15 Couch on Insurance 2d, §54.139* et seq.*)*. **Replacement cost or cost of repair standing alone is not sufficient proof of actual cash value. The amount for which the insurer may be held liable is the difference between the actual cash value of the property at the time just preceding the fire and the market value immediately after the fire** (*Molot, Inc. v. Commonwealth Ins. Co. of N.Y.*, 10 A.D.2d 683, 197 N.Y.S.2d 495). . . In this partial loss case plaintiff, by presenting evidence only of cost or repair, failed to submit sufficient evidence of "actual cash value" and the trial court properly dismissed that part of its claim relating to damage to the building. [Emphasis added.]

Incardona, 60 A.D.2d at 749-750.

To the same effect: *Agostino v. Holyoke Mut. Ins. Co.*, 89 A.D.2d 573, 452 N.Y.S. 2d 227 (2nd Dept. 1982) *leave to appeal denied* 57 N.Y. 2d 609, 457 N.Y.S. 2d 1025, 443 N.E. 2d 609.

The *Incardona* holding, requiring that the insured prove his loss by deducting the market value after the loss from the actual cash value before the loss, may be inconsistent with *Eshan* and *Gervant* and may be burdensome. While it based upon the principles of indemnification set forth in *McAnarney,* is good law and has not been overruled, it has been frequently distinguished and at times not followed.

Incardona was not mentioned, but not followed in *Allstate v. Kleveno,* 81 A.D. 2d 648, 438 N.Y.S. 2d 384, (2nd Dept. 1981) (after loss value not considered, however this was a total loss for which *Incardona* is inapplicable.) *Kates v. N.Y. Prop. Ins. Und. Assoc*, 128 A.D.2d 838, 513 N.Y.S.2d 757 (2nd Dept. 1987) distinguished *Incardona* on the grounds that it did not apply to a total loss.

In *Gumbs v. N.Y. Prop Ins. Und. Assoc.*, 114 A.D.2d 933, 495 N.Y.S. 2d 204 (2nd Dept. 1985) the insured offered evidence of the cost to repair his fire damaged premises and rested. The insurer moved to dismiss, based upon *Incardona.* In response, the trial court allowed the insured to re-open his case and offer testimony of a real estate appraiser, who inspected the property for the first time just before his testimony and provided testimony that was consistent with the cost of repairs. The Second Department noted that "[a]lthough it might be argued that Brunswick [the appraiser] had simply trotted out Englehardt's [the repair cost expert] $39,508 cost-of-repair figure but now presented it in the clothing of before and after valuations...those matters affecting the weight of credibility of Brunswick's evidence, not its legal sufficiency." Hence, although the trial court directed a verdict for the insurer, the Second Department reversed, holding that the *Incardona* proof was satisfied and granted a new trial.

Incardona was at criticized head on by Judge Richard S. Lane of Civil N.Y. in *Esperance v. Royal Globe,* 134 Misc. 2d 718, 512 N.Y.S.2d 313 (1987):

> The *Incardona* rule is simply wrong conceptually; see Comment* 2, NY Pattern Jury Instructions # 4:49. It borrowed a tort concept of damages from a personal property case where it may well have been appropriate-fire damaged furs retained and disposed of by the insured (*Molot v. Commonwealth Ins. Co.,* 10 A.D.2d 683, 197 N.Y.S.2d 495). It introduced that concept into a contract case, where it was not only inappropriate and unnecessary, but was excluded by any fair reading of the remedy that was carefully crafted by the parties and expressed with elegant simplicity. Furthermore, the concept enshrines market value as the determining factor despite explicit language to the contrary from the Court of Appeals; *McAnarney v. Newark Fire Insurance Co.,* 247 N.Y. 176, 159 N.E. 902.
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> Not only is the *Incardona* rule wrong conceptually, but it is an illuminating example of the trouble you get into when you try to fix something that isn't broken. For a century or more, cases of partial fire damage covered by the standard insurance policy have been easily resolved in terms of widely accepted and understandable accounting procedures. Only when one party or another was being unreasonable with respect to figures did a case reach the trial stage. Now, maybe, there will be a wild card-fair market value immediately after the fire. Rare will be the case in which a meaningful fair market value can be fixed. Unless the fire had devastated a large area, there will be no comparable sales, and, with income interrupted, capitalization and other income and book value approaches will be virtually useless.
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> If the problem created by the *Incardona* rule can be avoided by the simple expedient adopted by the insured's expert in the *Gumbs* case, *supra,* there will be "a lot of sound and fury signifying nothing." Counsel for insureds will simply have to learn a new trick, and a few uninitiated will get hurt. If not, experts will have another field day testifying in amorphous unintelligible concepts, and laymen-litigants and jurors alike-will be reminded of Mr. Bumble's famous words.
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> Wrong or impractical or both, am I commanded to follow the *Incardona* rule since neither the First Department, nor any other appellate court has spoken directly to the issue? I think not. There is a long and unbroken history in the First Department as to how these cases are to be decided. Furthermore, that history is supported by the authority of the Court of Appeals.

Esperance, 134 Mis. 2d at 720.

Unfortunately for those critics of the *Incardona* holding, this decision was not appealed and therefore not affirmed and has no *stare decisis* affect.

Insured's Right to Replacement Cost

Modern policies of insurance contain replacement cost provisions to the effect that the insured is entitled to the full replacement cost of the damaged premises if he repairs or replaces the property as soon as possible at the insured location. Typically, if the insured does not repair or replace the property as soon as possible, it is entitled to recover only the actual cash value of the loss. Hence when adjusting a loss, the parties must agree upon the actual cash value and the replacement cost. The actual cash value is paid upon agreement of the parties and the difference between actual cash value and replacement cost, consisting of the depreciation factor, is withheld and released after the repairs are completed and the insured establishes that it has spent at least as much as the full replacement cost to repair or replace the premises. This withheld sum is known as the "holdback". However, the insured's right to full replacement coverage and his right to recover the holdback has raised various legal issues, some of which have not been fully resolved.

In *Kumar v. Travelers Ins. Co.,* 211 A.D.2d 128, 627 N.Y.S.2d 185 (4th Dept. 1995), the insureds were covered by a homeowners policy that provided "guaranteed replacement cost", i.e., coverage in excess of policy limits, if they repaired or replaced the insured premises on the same location. The insureds were a married couple that were separated. Husband had acquired a separate home before the loss. After the loss

by fire to the insured premises, the Company paid policy limits. Wife acquired a new home for less than the policy limits. The insured's claimed the right to the full replacement cost of the husband's new home, acquired before the loss plus the wife's purchase price of her new home made after loss. The combined expenditure exceeded policy limits. The court held that the husband's new home couldn't be considered a replacement home for the damaged property because he acquired it before the loss. The cost of the wife's new home did not exceed policy limits and therefore she was not entitled to recover policy limits.

Kumar is significant in its interpretation of the standard clause in replacement cost coverage, requiring the insured's to rebuild on the same premises. The court held that this requirement does not mean that the insured's must actually rebuild on the same premises. Rather, it limits recovery for replacement cost to the hypothetical amount it would have cost to rebuild on said premises:

> Thus, we conclude that Travelers' agreement to pay the full cost to repair or replace the damaged dwelling with equivalent construction on the same premises merely establishes the limits of coverage and that replacement cost under the "GUARANTEED REPLACEMENT COVERAGE" provision is measured by what it would cost to replace the damaged structure on the same premises. The insured is not required, however, to replace the damaged dwelling on the same premises in order to recover replacement cost.
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> *Kumar* at 132.

In *Harrington v Amica Mut. Ins. Co.*, 233 A.D.2d 222, 645 N.Y.S.2d 221 (4th Dept. 1996) the insured was covered under a homeowners policy for the lesser of (a) the actual cash value, (b) the amount actually spent in repairing or replacing the damaged home or (c) the policy limits. The loss was adjusted by payment of the actual cash value with

an agreed holdback. The insured then entered into a land contract with a third party, selling the land upon which the insured property was located. The purchaser acknowledged that the home was damaged and undertook to make repairs. If the purchaser defaulted in making payment on the land contract, the home, including the improvements made by the purchaser, would revert to the insured. Thus, although the property was sold, the insured maintained an insurable interest in the property.

After the purchaser repaired the premises the insured made claim for the holdback and the insurer denied coverage therefor. The court held that since the insured did not expend anything in making the repairs and since he did not replace the premises as his home, he was not entitled to recover the holdback:

> Plaintiff contends in his complaint and his affidavit in support of his motion that he is entitled to recover the amount of defendant's estimate of replacement costs once Lindow completed the repairs. Plaintiff's contention ignores several facts. First, plaintiff had no ****224** "costs"--he spent nothing to replace the dwelling. Second, the new structure does not "replace" plaintiff's home; plaintiff does not live there. Third, plaintiff did not need to rebuild on the premises, and has never indicated that he intends to rebuild elsewhere (*see, Kumar v. Travelers Ins. Co.*, 211 A.D.2d 128, 627 N.Y.S.2d 185).

Harrington at 223-224

In *Bartholomew v. Sterling Ins. Co.*, 34 A.D.3d 1157, 825 N.Y.S.2d 795 (3rd Dept. 2006), the insured made a claim under a policy that provided coverage for replacement cost upon completion of repairs or replacement of the property. The insured accepted the actual cash value of the property, made repairs and made claim for the holdback. The insured apparently made many of the repairs by himself and did not have itemized paid bills to establish the replacement cost. The court held that the insured was not

entitled to replacement cost for failure to document his repair expenses.

There is some dispute as to whether the insured is entitled to replacement cost if he does not replace the property when the insurance company denied coverage and refused to offer actual cash value. A controversial federal court case, *Zaitcheck v. American Motorists Ins. Co.*, 554 F.Supp. 209 (S.D.N.Y. 1982), held that where the insurance company wrongfully denied coverage to two elderly school teachers who had no means to rebuild or ability to finance rebuilding costs, the insurer was estopped from requiring the insureds to rebuild before they were entitled to recover replacement cost. Hence, replacement cost was awarded even though the insureds had not rebuilt the damaged premises. The court held:

> ***217** I find that both case law and equitable considerations render replacement cost the appropriate method of valuing plaintiffs' damages. The defendant does not challenge the plaintiffs' contention that a bank would be chary to lend money on the basis of an unlitigated law suit in which the defendant and its vast resources intend to present several defenses to payment. Nonetheless, defendant asserts, case law precludes plaintiffs' recovery of replacement value, citing *American Universal Ins. Co. v. Falzone,* 644 F.2d 65 (1st Cir.1981); *Kolls v. Aetna Cas. & Sur. Co.,* 503 F.2d 569 (8th Cir.1974); *Lerer Realty Corp. v. M.F.B. Mutual Ins. Co.,* 474 F.2d 410 (5th Cir.1973); *Bourazak v. North River Ins. Co.,* 379 F.2d 530 (7th Cir.1967); *Higgins v. Ins. Co. of North America,* 256 Or. 151, 469 P.2d 766 (1970).[FN11] These cited cases, however, are distinguishable from the instant case. In all the relevant cases cited by defendant save *Lerer Realty,* the defendant paid actual cash value, and was only litigating the issue of whether additional monies would be due under the relevant replacement cost contract provisos.[FN12] Thus, plaintiffs in the cited cases had at least some money with which to begin rebuilding their property.
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> The language of the Zaitchicks' insurance contract also supports my emphasis on whether cash value has been paid or not. The contract states that "[t]he Named Insured may elect to disregard this [replacement cost] condition in making claim hereunder, but such election shall not prejudice the Named Insured's right to make further claim within 180 days after loss for any additional liability [for replacement cost]." Defendant's

> Exhibit M, "Additional Conditions," ¶ 1(f). In other words, insureds can obtain the necessary funds to begin rebuilding their home, and subsequently upon completion of the construction, obtain additional amounts up to the replacement value. In the instant case, plaintiffs were refused any monies under the insurance contract. Not surprisingly, they were unable to replace their home. This conduct by defendant made it impossible for plaintiffs to fulfill the condition precedent, and therefore, excuses plaintiffs from performance of the replacement condition.

Zaitchick at 217

Zaitchick has been criticized and not followed by other courts. Refusing to require proof that the insured actually repaired or replaced the property before awarding replacement cost could result in a winfall to the insured in contravention to the well-established principles of indemnification. Thus, in another federal case, decided by the Third Circuit under New York law, *Dickler v. CIGNA Prop. & Cas. Co.,* 957 F.2d 1088 (3rd Cir. 1992), *Zaitchick* holding was respectfully rejected:

> While the logic of *Zaitchick* has much to commend it, we do not believe that *Zaitchick* justifies a replacement cost award in our case. First, *Zaitchick* was decided by a federal district court pursuant to its diversity jurisdiction and consequently has no precedential value and cannot serve to justify a departure from the clear contractual language of CIGNA's policy. Second, in the absence of New York authority allowing payment of replacement cost without repairs, we do not find *Zaitchick* persuasive in the present context. Finally, the equities in *Zaitchick* were far different from the equities in our case: *Zaitchick* involved an elderly couple whose only home was destroyed by fire, whereas our case takes place in a commercial setting and involves relatively sophisticated parties. The windfall that the Dickler Group would enjoy if awarded full replacement cost without rebuilding had no parallel in *Zaitchick.*

Dickler at 1095-1096.

Those in favor of the *Zatchick* holding (if the insurer denies coverage, it cannot insist upon requiring the insured repair or rebuild to qualify for replacement cost) in the

First Department case of *438 Manhattan Ave. Inc. v. Ins. Co., of the State of Penna.*, 251 A.D.2d 71, 673 N.Y.S.2d 687 (1st Dept. 1998) which held:

> With regard to damages, we agree with the IAS court that the insurer was barred from asserting policy language limiting replacement cost by its refusal letter repudiating the policy (*see, Igbara Realty Corp. v. New York Property Ins. Underwriting Assoc.*, 63 N.Y.2d 201, 217, 481 N.Y.S.2d 60, 470 N.E.2d 858) and by its failure to raise the issue promptly.

This case, at best, leaves the question open. The decision appears to be based upon the fact that the insurer did not notify the insured that its coverage is limited to actual cash value in the letter denying coverage or in its affirmative defenses asserted in the answer. Had it done so, the mere fact the insurer denied coverage without paying actual cash value would not, it would seem, have precluded the enforcement of the requirement that repairs be made and paid for before replacement cost coverage is allowed.

The better-reasoned decisions, in the opinion of this writer, are found in *Todd v. Wayne Coop. Ins.*, 31 A.D.3d 1026, 819 N.Y.S.2d 179 (3rd Dept. 2006) and *Dr. Watson Holdings, LLC v. Caliber One Indem. Co.*, 15 A.D.3d 1969, 789 N.Y.S.2d 787 (4th Dept. 2006).

In these decisions, after finding for the insureds, the Courts awarded actual cash value and permitted the insureds to reapply to the carrier for the holdback after repairs are completed. By awarding actual cash value and by maintaining jurisdiction until repairs are completed, and then by making a subsequent award if the insureds comply with the policy requirements, the courts enforced the policy terms and accomplished the goals of indemnification to the benefit of all parties.

CONCLUSION

The notion that property insurance is indemnity insurance, with the goal of placing the insured in the same position he or she would have been had the loss not occurred, has been the law for centuries. The broad evidence rule of *McAnanerny*, adopted 79 years ago and very much alive today, is the mechanism employed to achieve this goal by allowing and requiring that an unlimited array of proof, having any bearing upon valuation, be presented and considered by the judge, jury or appraisers who are determining the amount of an insured's recovery.

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