

IN THE SUPREME COURT STATE OF ARIZONA

GERALD WALKER, III,
and ADA WALKER,
Plaintiffs,

v.

AUTO-OWNERS INSURANCE
COMPANY, a foreign company,
Defendants.

No. CV-21-0236-CQ

United States District Court
No. 4-20-cv-00449-TUC-CKJ

UNITED POLICYHOLDERS' AMICUS CURIAE BRIEF

Thomas B. Dixon
Dixon Law Offices, P.L.C.
343 W. Roosevelt St., Suite 200
Phoenix, Arizona 85003
602.258.8400
tom@dixonlawoffices.com

*Attorney for Amicus Curiae
United Policyholders*

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STATEMENT OF INTEREST OF *AMICUS CURIAE*

UP is a non-profit organization whose mission is to serve as an effective voice and a source of information and guidance for insurance commercial and personal lines around the country. UP is funded by donations and grants. It does not sell insurance or accept money from insurance companies. Unlike insurers, individual policyholders are not repeat players on insurance coverage issues. UP works to provide an intellectual counterweight to the claims of the insurance industry, in order to help facilitate the evenhanded development of insurance law. Indeed, the Illinois Supreme Court recently favorably cited a UP *amicus curiae* brief on the labor depreciation issue that is before this Court. *Sproull v. State Farm Fire & Cas. Co.*, 2021 IL 126446 ¶ 53. Multiple state supreme courts as well as the U.S. Supreme Court have similarly cited UP briefs with approval on other subjects.¹ Because the issues in this case go to the very heart of Arizona insurance commercial and personal lines consumers' rights, they fall squarely within UP's advocacy interests. UP's library of publications, tools and guidance includes many publications that address the topic of proper and improper depreciation. *See, e.g.*, "Depreciation Basics" at <https://www.uphelp.org/pubs/depreciation-basics>.

¹ *See, e.g., Humana Inc. v. Forsyth*, 525 U.S. 299, 314 (1999); *Cont'l Ins. Co. v. Honeywell Int'l, Inc.*, 234 N.J. 23, 64 (2018); *Allstate Prop. & Cas. Ins. Co. v. Wolfe*, 629 Pa. 444, 452–53 (2014); *Julian v. Hartford Underwriters Ins. Co.*, 45 Cal. 4th 747, 760 (2005).

INTRODUCTION

Approximately fifty percent of insurance carriers *do not* engage in the practice of depreciating labor costs. *See Arnold v. State Farm Fire and Cas. Co.*, 268 F.Supp.3d 1297, 1312 n.23 (S.D. Ala. 2017) (“some adjusters believe only the material and not the labor should be depreciated”). Of the approximately fifty percent of the carriers engaging in the practice, many have filed and use coverage forms expressly authorizing the practice. *Hicks v. State Farm Fire & Cas. Co.*, 751 F. App’x. 703, 709 (6th Cir. Oct. 15, 2018), *reh’g denied* (Nov. 21, 2018) (“State Farm reworded its standard homeowner’s insurance policies in Arkansas to expressly depreciate labor and material cost, consistent with Arkansas law”). Expressly disclosing the practice of depreciating labor in an insurance policy creates clarity and transparency as policyholders clearly know what they are purchasing and how a claim will be calculated.

This case deals with a practice that the *minority* of insurance companies engage in: depreciating labor costs without a policy that expressly authorizes the practice. Auto-Owners is well aware of the controversy of depreciating labor costs as it has been party to similar cases around the country. Indeed, in 2019 the Tennessee Supreme Court, interpreting a policy with an actual cash value (“ACV”) provision identical to Plaintiffs’ here, rejected Auto-Owners’ argument that “deduction for depreciation” was not ambiguous and “that depreciation of a property

is taken from the total replacement cost, which includes both labor and materials.” *Lammert v. Auto-Owners (Mutual) Ins. Co.*, 572 S.W.3d 170, 173 (Tenn. 2019). Rather than being transparent with Arizona policyholders by expressly disclosing that it was depreciating labor costs when calculating claims, Auto-Owners engaged in this practice without informing its policyholders.

Ultimately, the question of whether labor should be depreciated in determining ACV requires interpretation of the insurance contracts themselves. As such, the issue is a question of law for the Court.

Arizona law honors and enforces the principle that insurance policies should be interpreted to effectuate indemnity and uphold policyholders’ reasonable expectations of coverage. *See Apollo Ed. Group, Inc. v. Nat’l Union Fire Ins. Co.*, 250 Ariz. 408, 412 (2021). Consistent with those principles, labor costs should not be depreciated. Depreciation of labor results in policyholders not receiving the full amount that they reasonably are entitled to under their ACV coverage. It also often results in policyholders being unable to collect replacement cost value (“RCV”) benefits for which they have paid an additional premium. That can lead to a life-changing loss for policyholders, and a windfall for the insurer.

ARGUMENT

I. MEANING OF THE TERMS ACTUAL CASH VALUE, REPLACEMENT COST VALUE, AND DEPRECIATION.

Determining whether labor should be depreciated depends on the evaluation

of unique property insurance concepts and coverages, such as those contained in Plaintiffs' policies at issue in this case.

Actual Cash Value

The precise interpretation of ACV is at the heart of this dispute. Generally, ACV is the amount required to put a policyholder back to where he or she was before the loss. *Hicks*, 751 F. App'x. at 706-07 (explaining ACV coverage). ACV coverage is "pure indemnity coverage." *Travelers Indem. Co. v. Armstrong*, 442 N.E.2d 349, 352 (Ind. 1982). To indemnify "means simply to place the insured back in the position she enjoyed prior to the loss." Johnny Parker, *Replacement Cost Coverage: A Legal Primer*, 34 WAKE FOREST L. REV. 295, 296 (1999). Its purpose "is to make the insured whole but never to benefit him because a [loss] occurred." *Armstrong*, 442 N.E.2d at 352. The obvious corollary to this principle is that the ACV approach should never underpay a claim by providing less than indemnity.

"[A]ctual cash value' does not mean that the determination is some sort of free-for-all" where the adjuster chooses "any calculation of his or her choosing based on nothing more than feelings. If that were the case, it would be difficult to understand why any reasonable person would buy insurance." *Coppins v. Allstate Indem. Co.*, 359 N.W.2d 896, 905 (Wis. Ct. App. 2014). A policyholder should reasonably expect that ACV provides enough money to return a destroyed structure to a reasonable standard of livability.

For example, if a policyholder owned a house with a ten-year-old roof destroyed by hail, ACV would be the price of providing the policyholder a ten-year-old roof that was not destroyed by hail. Disputes arise, as here, because it is not possible to buy a ten-year-old roof (or ten-year-old roofing materials) to install on an existing building. This dilemma has led to various methods of attempting to value the cost of putting policyholders back in the position they were in prior to the loss.

Replacement Cost Value

In contrast to ACV (which provides enough money to return damaged property to the same condition it was in immediately before a casualty), RCV coverage allows a policyholder to recover full repair costs with all new construction materials. “Replacement cost coverage, therefore, in contravention of the general rule that an insured cannot profit through insurance, *results in the insured being better off than he or she was prior to the loss, since the insured ends up with a more valuable property.*” Allan D. Windt, 3 INS. CLAIMS AND DISPUTES § 11:35 (6th ed. Mar. 2021 Update) (emphasis added).

In other words, using the above example of a ten-year-old roof, replacement cost coverage will pay for the cost of a *new* roof, as opposed to the ten-year-old roof destroyed by hail. Because RCV coverage places policyholders in a *better* position than before the loss (they now have a new roof rather than a ten-year-old roof), it is not indemnity coverage. Policyholders must pay an additional premium for

replacement cost coverage.

The timing of ACV and RCV payments differs. ACV benefits are paid as soon after the loss as the amount owed by the insurance company is determined. In contrast, RCV benefits are typically reimbursed to the policyholder *if and when* repairs have been substantially completed and paid for by the policyholder, and only if the repairs are completed within a specified period of time after the loss. Steven Plitt, *et al.*, COUCH ON INSURANCE §176:56 (3d ed. Dec. 2021 Update). As the recovery of RCV benefits requires an insured to take additional steps, insurers may try to allocate as much of the loss as possible into replacement cost coverage rather than ACV to make it less likely the insurer will have to pay any replacement costs.

Depreciation

Depreciation is “the amount an item has lessened in value since it was purchased, taking into account age, wear and tear, market conditions, and obsolescence. Although depreciation has been defined in several ways, *the principal definition attributable to that term refers to ‘physical deterioration.’*” Richard J. Cohen, *et al.*, 5 NEW APPLEMAN ON INS. LAW LIBRARY ED. §47.04[2][a] (2021) (emphasis added); *Black’s Law Dictionary* (10th ed., 2014) (depreciation is “[a] reduction in the value or price of something; specif., a decline in an asset’s value because of use, wear, obsolescence, or age”). “Physical depreciation is a visible condition.” National Committee on Property Insurance, *Actual Cash Value*

Guidelines: Buildings, Personal Property (1982). Thus, the concept of depreciation considers that a ten-year-old roof is not valued the same as a new roof.

**Common law and policy methods of
determining actual cash value**

UP understands that the parties in this case agreed to calculate the ACV of the covered losses at issue by calculating RCV and deducting depreciation.² This is consistent with how the Arizona Department of Insurance and Financial Institutions (“ADOI”) informs Arizona commercial and personal lines consumers ACV is to be calculated: “Actual cash value” means “the cost to repair or replace the damaged property with materials of like kind and quality, less depreciation of the damaged property.” *See*

https://difi.az.gov/sites/default/files/documents/files/Homeowners_Check_Up_04%202015.pdf (last visited Feb. 3, 2022). The question that remains, however, is *what* should be depreciated in order to accomplish the intended purpose of indemnity under the replacement cost less depreciation methodology.

² Alternative methods of calculating actual cash value are the broad evidence rule and fair market value approaches. The broad evidence rule allows the fact-finder to consider any relevant factor to establish a correct estimate of the value of the damaged or destroyed property. *Hicks*, 751 F. App’x. at 706. As the Sixth Circuit explained in *Hicks*, where the replacement cost less depreciation methodology is used, “the instructive precedents [addressing labor depreciation] are not those from states that reject reproduction cost, but those that define actual cash value as replacement cost less depreciation, like Illinois, Ohio, and Alabama.” *Id.* at 711.

II. DEPRECIATION OF LABOR IS DIRECTLY CONTRARY TO THE CONCEPT OF INDEMNITY.

Under a replacement cost policy, the property is fully repaired with brand new materials and without any out-of-pocket loss by the insured except the deductible. In contrast, ACV puts the policyholder in the same condition as before the loss. Because physical material depreciation is withheld to determine the ACV (as both parties agree can and should be done), the policyholder bears all of the costs and expenses associated with all of the pre-loss physical wear and tear to the materials and leaves the policyholder as she was before the loss, no better and no worse – less the applicable deductible.

If additional amounts are withheld as depreciation for labor costs, the policyholder does not get ACV coverage because he or she is not restored to his or her pre-loss condition. He or she is no longer receiving ACV coverage, but something less.

A basic example illustrates the differences between RCV and ACV, the interplay between ACV and RCV, and the role of depreciation and its impact on labor. Assume a residential home has a ten-year-old shingled roof with a normal life span of twenty years is destroyed in a hurricane. Further assume that all of the shingles were properly installed at the time the policyholder buys ACV coverage.

Determining the replacement cost value is simple – it is the cost to replace all damaged components of the roof with brand new materials. Assume that the

undisputed replacement cost of the damaged roof in our hypothetical is \$30,000. To arrive at an actual cash value amount, the next step is to determine the proper depreciation. When determining the appropriate deduction for depreciation, it is critical to keep the goal of indemnity at the heart of the calculation, i.e., to restore the insured to his or her pre-loss condition. To do this, the goal must be to give the insured what he or she had before the loss — a ten-year-old properly installed roof. ACV therefore requires payment of the value of ten-year-old shingles already properly installed on the roof, because the policyholder's shingles were already installed on the roof at the time of the loss. The shingles were not sitting in a garage.

So how is this accomplished? First, the damaged ten-year-old shingles must be removed and disposed of, and that labor cost must be ascertained. Then the diminished value of ten-year-old shingles at the time of the loss must be determined. Finally, the labor cost of re-installing shingles back to the same way they were installed before the loss must be calculated. This calculation puts the insured right back where she was before the loss (*i.e.*, a residential home with installed shingles minus the full cost of the pre-loss wear and tear of the shingles). The policyholder in this hypothetical is *not* receiving replacement cost coverage or a windfall because he or she must fully pay, out of his or her own pocket, the difference between ten-year-old shingles and brand-new shingles and the deductible. The physical depreciation fairly penalized the policyholder for the roof's pre-loss wear and tear.

Practically, there is no market for ten-year-old shingles and no store sells “used” ten-year-old shingles. As a result, the concept of depreciation was born to hypothetically determine what the cost of those materials would be. In the above hypothetical, if we simplistically assumed the cost of the \$30,000 roof was half labor (\$15,000) and half materials (\$15,000), then the proper ACV payment would be 100% of the labor costs (\$15,000) and half of the material costs due to the 50% depreciation of the shingles (\$7,500), resulting in a total ACV payment of \$22,500.

In contrast, if labor was also depreciated by 50%, the ACV payment would decrease to \$15,000. The policyholder would not have enough money to return the property to pre-loss condition. *See Lammert, 572 S.W.3d at 175* (using a similar “hypothetical [to] illustrate[] the dilemma”).

Furthermore, if the labor for removing the damaged shingles and re-installing replacement shingles is also withheld in part, this leaves the policyholder in a worse position because even if he or she can afford to pay the difference between the worn ten-year-old shingles and brand-new shingles out-of-pocket, the ACV payment does not enable the insured to remove the damaged shingles and reinstall the shingles paid for. This double deduction does not accomplish indemnity and is the ultimate reason why Auto-Owners’ logic and arguments fail. Auto-Owners’ theory leaves the insured in a worse condition than before the loss, thus not resulting in indemnity.

III. THE QUESTION OF WHETHER LABOR SHOULD BE DEPRECIATED IS A MATTER OF CONTRACT INTERPRETATION AND SHOULD BE DECIDED AS A MATTER OF LAW.

Insurance policies are interpreted as a matter of law and are subject to the general rules of contract construction. *Sparks v. Republic Nat. Life Ins. Co.*, 132 Ariz. 529, 534 (1982). The resolution of whether labor costs should be depreciated is not a question of fact, but a question of law appropriate for a court's independent determination. *Id.* There is no dispute in this case that the Court can determine whether insurers in Arizona can depreciate labor costs from an ACV payment when ACV is not defined in the applicable insurance policy.

Even if the depreciation of labor question could be determined as a matter of fact instead of a matter of law, this may have profound and adverse consequences to policyholders. The harmful effect is that factfinders could render opposite awards to policyholders in identical situations, resulting in *different* ACV benefits.

Worse, some insurers might across the board insist on depreciating labor when making a settlement offer. Many homeowners do not have the knowledge or resources to argue that doing so is incorrect. Thus, this issue should be decided as a matter of law to provide certainty and clarity to policyholders *and* insurers.

IV. A REASONABLE CONSTRUCTION OF THE INSURANCE POLICIES AT ISSUE IS THAT LABOR SHOULD NOT BE DEPRECIATED.

Under Arizona law, an insurance policy that is ambiguous must be construed

in a manner most favorable to the insured. *Sparks*, 132 Ariz. at 535. A reasonable construction of the insurance policies in this case is that labor is *not* included in depreciation. Not only would depreciating labor costs require ignoring the definition of common words, doing so would also fail to effectuate the purpose of actual cash value coverage of indemnifying the policyholders for their losses.

Depreciation is defined by insurance law hornbooks, and *Black's Law Dictionary*, as a decrease in value because of factors including age, wear and tear, market conditions or value, and obsolescence. APPLEMAN §47.04[2][a]; *Black's Law Dictionary* (10th ed. 2014). The principal definition of depreciation “refers to ‘physical deterioration.’” APPLEMAN §47.04[2][a]. *Depreciation* is the “reduction in value of *tangible* property.” Robert J. Prah, *Introduction to Claims*, 87 (1988) (emphasis added). The depreciation factors of age, wear and tear, market conditions or value, and obsolescence can only apply to material, not labor. To the extent that labor is subject to market conditions, its value generally rises as wages go up. Labor is not a physical thing that can deteriorate.

Material is defined as: “1. A solid substance such as wood, plastic, metal, or paper. 2. The things that are used for making or doing something.” *Black's Law Dictionary* (10th ed. 2014). Labor is “[w]ork of any type.” *Id.* As the court explained in *Titan Exteriors, Inc. v. Certain Underwriters at Lloyd's, London*, 297 F. Supp.3d 628, 634 (N.D. Miss. 2018), “[l]abor does not suffer use, wear, or

obsolescence. It does not physically deteriorate.” *Id.* Thus, it is difficult to envision a scenario where labor would depreciate since it is not susceptible to aging or wear.

The National Underwriter Company publishes, under the name “FC & S”, a comprehensive library of reference books for insurance professionals. FC & S also provides online bulletins in which its experts respond to questions from insurance professionals. The bulletin is used by insurance agents and brokers to interpret standard insurance policy provisions. FC & S has stated its position is that depreciation should not apply to labor unless a policy explicitly states that it should. FC&S Bulletin, *Depreciation of Labor* (Nat’l Underwriting Co. Dec. 3, 2014).

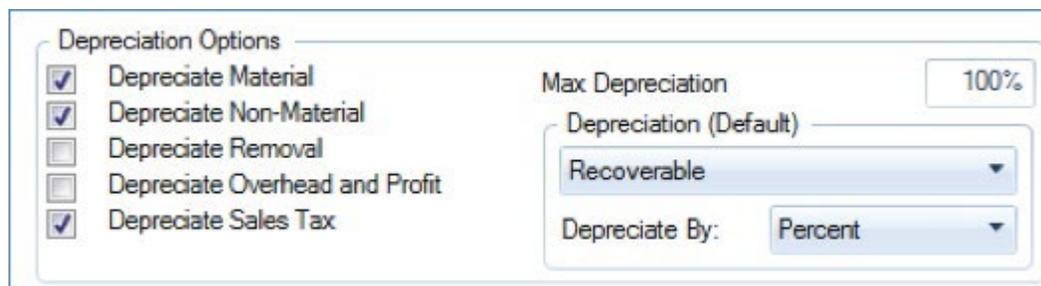
Auto-Owners should not be allowed to reap the benefit of a term that it chose not to define in their policies. Even the International Risk Management Institute (“IRMI”), an independent insurance industry entity that provides instruction to the insurance industry concerning the application of policy provisions, agrees. It has explained that if an insurance company wants its own interpretation of ACV to apply, it can simply define ACV in its own policy. *See* Mike McCracken, International Risk Management Institute, Inc. Expert Commentary, *What Exactly is Actual Cash Value? Better Yet, How Do You Calculate It?* (Sept. 2018), available at: <https://www.irmi.com/articles/expert-commentary/what-exactly-is-actual-cash-value> (last visited Feb. 3, 2022).

Auto-Owners could have easily defined ACV to include the depreciation of

labor. It chose not to do so. Auto-Owners should not now get the benefit of its affirmative decision not to define ACV in its policy. Many insurers have taken the simple step of defining ACV to include depreciation of labor costs. *See, e.g., Hicks*, 751 F. App'x. at 709. Many carriers also choose simply not to depreciate labor costs.

Tellingly, the claims adjusting software that is almost universally used by insurance carriers further demonstrates that it is reasonable for an insured to expect labor costs will not be depreciated. The top four software packages used by insurance companies to adjust structural damage claims all allow the insurance company to select whether or not to depreciate labor costs when calculating ACV.

For example, Xactimate® by Xactware, is a software program for estimating construction and repair costs that is widely used by “22 of the top 25 property insurance companies in the U.S. and 10 of the top 10 Canadian insurers....”³ The below Xactimate® screenshot shows that an insurer can choose to select or de-select “Depreciate Non-Material” or “Depreciate Removal,” both of which are labor items:



³ *See* <https://www.xactware.com/en-us/company/about/#> (last visited February 3, 2022).

http://xactimate.xactware.help/help_baggage/2015_WhitePaper_CalculatingDepreciationForStructuralPropLines.pdf (last visited February 3, 2022). Given that insurance companies' own valuation software allows for the depreciation of labor costs or not, Auto-Owners cannot credibly argue that Plaintiffs' policy interpretation is unreasonable. *See Sproull*, 2021 IL 126446, ¶¶ 52-53 (distinguishing cases that failed to recognize both industry practice and standard software allow insurance companies to decide whether or not to depreciate labor).

To create certainty and clarity in the insurance marketplace for insurers and policyholders, some states and courts have sought to require insurers to specify that they will depreciate labor costs in calculating ACV. For example, in 2017, the Mississippi Commissioner of Insurance issued a bulletin instructing insurers to, among other things, “clearly provide for the depreciation of labor in the insurance policy.”⁴ Similarly, after determining that State Farm's Kentucky homeowner's policy did not allow State Farm to depreciate labor costs, the Sixth Circuit explained that “following [its] decision, State Farm can ensure that the wording of any new homeowner's insurance policy it offers in Kentucky defines ACV depreciation to include both labor and materials.” *Hicks*, 751 F. App'x. at 709. To the extent this Court determines that an insurer may depreciate labor costs when calculating ACV

⁴ *See* <https://www.mid.ms.gov/legal/bulletins/20178bul.pdf> (last visited February 3, 2022).

in Arizona, the Court should, at a minimum, require insurers to specifically disclose in their policies that labor will be subject to depreciation.

Auto-Owners should not benefit by deducting labor from the policyholder's ACV payment. As explained below, even if the term is subject to more than one reasonable interpretation, rules of construction favor the policyholders' position.

Finally, depreciating labor would not effectuate the purpose of ACV coverage, *i.e.*, indemnity, or placing policyholders back in the position they enjoyed prior to the loss. While ACV coverage can never return the policyholders to the *precise* position they were in prior to the loss, insureds need enough money to repair or replace the damaged property, including installation.

Consider again the policyholders in the earlier example with a ten-year-old roof that was destroyed by a storm. The only way to return the policyholders back to the exact position they were in before the loss would be to install a ten-year-old roof. That, however, is not feasible. Therefore, ACV benefits provide the policyholders the cost of a new roof, depreciated by the amount that their roof has deteriorated. But if the insurer also depreciates the cost of labor, insureds will not receive enough money to install the roof. Before the loss, the insureds had a ten-year-old roof that was *installed* on the house. To be made whole, the insurer must pay enough money to *install* a ten-year-old roof on the insured's house. Whether installing a new roof or a ten-year-old roof, the price of labor is the same.

Depreciating labor will not make the policyholder whole and will frustrate the indemnity purpose of the actual cash value coverage: indemnification.

V. TO THE EXTENT THE POLICY TERMS “ACTUAL CASH VALUE” AND “DEPRECIATION” ARE SUBJECT TO MORE THAN ONE REASONABLE INTERPRETATION, THE POLICY MUST BE INTERPRETED IN FAVOR OF THE POLICYHOLDERS.

“Where the language is unclear and can be reasonably construed in more than one sense, an ambiguity is said to exist and such ambiguity will be construed against the insurer. In determining whether an ambiguity exists in a policy, the language should be examined from the viewpoint of one not trained in law or in the insurance business.”

Sparks, 132 Ariz. at 534 (citations omitted). The same principles apply here. The Tennessee Supreme Court addressed an Auto-Owners policy that contained the identical language to Plaintiffs’ here—*i.e.*, the policy did “not define actual cash value but states that actual cash value includes a deduction for depreciation.” *Lammert*, 572 S.W.3d at 173; *see also* Dkt. 26, at 3 (“... we shall pay the actual cash value of the property at the time of loss. Actual cash value includes a deduction of depreciation.”) The court held this language—also contained in Plaintiffs’ policy here—is subject to more than one reasonable interpretation. *Lammert*, 572 S.W.3d at 173, 179. Thus, the court “strictly construed [it] against the insurance companies and in favor of the insured[.]” and held that “labor may not be depreciated when the insurance company calculates the actual cash value of a property using the replacement cost less depreciation method.” *Id* at 179.

Similarly, in *Sproull* the Illinois Supreme Court held that a policy that failed

to define ACV or depreciation was ambiguous, and did not allow depreciation of labor costs. *Sproull*, 2021 IL 126446, ¶ 54. In *Hicks*, the Sixth Circuit was faced with a policy that defined ACV as replacement cost less depreciation. *Hicks*, 751 F. App'x. at 711. The court determined that a “layperson confronted with [this] policy could reasonably interpret the term depreciation to include only the cost of materials” and thus held that the policy did not allow State Farm to depreciate labor costs. *Id.* at 709. Other courts are in accord. *E.g.*, *Lains v. American Family Ins. Co.*, 2016 WL 4533075 (W.D. Wash. Feb. 9, 2016) (“The policy does not define depreciation ... the language is ambiguous”); *Arnold*, 268 F.Supp.3d at 1309 (“a reasonable insured in the plaintiff’s position, not possessing specialized knowledge or expertise about such matters and knowing only the Policy language and the common, everyday meaning of the language employed, could reasonably understand that ACV does not include depreciation of labor”).

It is unreasonable to assume insureds would be able to infer labor would depreciate from an ACV coverage policy when the term “actual cash value” is not defined. *See* Adam J. Babinat, *Ensuring Indemnity: Why Insurers Should Cease The Practice of Depreciating Labor*, 22 DRAKE J. AGRIC. L. 65, 78, 85 (Spring 2017) (to protect farmers, recommending that Iowa adopt a regulation similar to California that the expense of labor to repair, build or replace damaged property is not a component of physical depreciation). Here, answering the first certified question in

favor of Auto-Owners's interpretation would place an unfair burden on the insureds, and unjustly enrich Auto-Owners. *Id.* at 78.

Moreover, allowing insurers to depreciate labor is contrary to the reasonable expectations of their customers and tends to cause them significant financial harm. The reasonable expectation of the policyholders is that the indemnity policy they purchased will provide coverage sufficient to actually indemnify them or put them back in the position they were in prior to the loss.

The harm to policyholders and the windfall to insurers from depreciating labor is obvious with respect to policies that only provide ACV coverage, and do not include RCV coverage. Depreciating labor costs means that insurers will *never* pay the cost of labor, and policyholders will never receive that portion of their loss.

Many insurance policies also include RCV coverage, for which policyholders pay an additional premium. Even when RCV coverage exists, it is not as simple as the insurer paying whatever amount it has calculated as depreciation on labor as replacement cost coverage rather than ACV coverage. In fact, where the policyholders have paid for replacement cost coverage, depreciating labor in the calculation of ACV will often result in an even bigger windfall for the insurer than where there is no replacement cost coverage. Furthermore, the insurer has received the extra premium without paying the benefit to the insured.

Standard property insurance policies provide that replacement cost coverage

is not paid until the repairs have actually been made. Moreover, those repairs must be completed within a specified time, in some cases as little as 180 days after payment of the actual cash value, or replacement cost coverage is forfeited. *See Sher v. Allstate Ins. Co.*, 947 F. Supp. 2d 370 (S.D.N.Y. 2013).

When an insurer retains amounts for depreciation of labor and pays less in ACV coverage, it is likely the policyholder will not have enough funds to rebuild the damaged property within the policy's required time period, or at all. In that instance, the insurer *never pays* the replacement cost coverage for which the policyholders contracted and paid. The insurer receives a windfall. The policyholders remain without a roof.

Even if policyholders manage to save enough money to make repairs and eventually receive replacement cost value benefits from the insurer, in the interim, the insurer has earned income on the withheld depreciation. Meanwhile, the policyholders have been denied the use of those funds when they may need them the most (to pay their contractors.)

CONCLUSION

For the foregoing reasons, United Policyholders respectfully requests that the Court answer the certified question in a manner that does not permit Auto-Owners or other insurers to depreciate labor costs from ACV payments when the policy does not expressly authorize it.

Respectfully submitted,

/s/ Thomas B. Dixon

Thomas B. Dixon

Dixon Law Offices, P.L.C.

343 W. Roosevelt St., Suite 200

Phoenix, Arizona 85003

602.258.8400

tom@dixonlawoffices.com

Attorney for Amicus Curiae

United Policyholders