

IN THE SUPREME COURT OF PENNSYLVANIA  
EASTERN DISTRICT

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NO. 12 EAP 2019  
NO. 13 EAP 2019

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KONRAD KURACH, APPELLANT  
v.  
TRUCK INSURANCE EXCHANGE, APPELLEE  
and  
MARK WINTERSTEIN, et al, APPELLANT  
v.  
TRUCK INSURANCE EXCHANGE, APPELLEE

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**BRIEF OF AMICUS CURIAE UNITED POLICYHOLDERS  
IN SUPPORT OF PETITIONERS-APPELLANTS**

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On Appeal from the Judgment of the Superior Court Filed August 24, 2018, at No. 1726 EDA 2017 (reargument denied October 10, 2018) reversing the Order entered on April 21, 2017 and remanding to the Court of Common Pleas, Philadelphia County, Civil Division at Nos. 00339 and 03543 July Term, 2015.

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## **I. STATEMENT OF INTEREST OF AMICUS CURIAE**

Amicus curiae United Policyholders (“UP”) submits this brief to support the position of Petitioners-Appellants, Konrad Kurach and Mark Wintersteen (“Petitioners” or “Appellants”), who are insured under property insurance policies issued by Truck Insurance Exchange (“Truck”). UP’s efforts can assist both the attorneys and this Court by focusing on public policy considerations surrounding the analysis of whether general contractor overhead and profit (“GCOP”) should be excluded in the context of reaching an actual cash value adjustment of a property insurance claim.

UP is a non-profit public interest consumer advocacy organization dedicated to helping preserve the integrity of the insurance system. Since 1991, UP has provided insurance guidance to disaster victims, individuals and businesses and been an advocate for insurance consumers throughout the United States. UP’s work is supported by donations, grants, and volunteer labor. UP does not sell insurance or accept funding from insurance companies.

Through its *Advocacy and Action Program*, UP regularly engages with regulators, legislators, academics, journalists and stakeholders on legal and marketplace developments relevant to all policyholders and all lines of insurance. UP’s Executive Director is an official consumer representative to the National

Association of Insurance Commissioners. The organization coordinates with and assists insurance regulators in Pennsylvania in solving consumer problems.

Much of UP's work is aimed at helping individuals and businesses purchase appropriate insurance, and repair, rebuild, and recover after disasters through its *Roadmap to Preparedness* and *Roadmap to Recovery Programs*. During its work in disaster areas, UP has developed extensive knowledge of actual cash value coverage in first-party property insurance policies. UP has a vital interest in seeing that first-party property insurance policies sold to countless policyholders, in Pennsylvania and elsewhere, are interpreted properly and consistently by insurance companies and the courts.

When insurance companies reduce claim payouts by failing to include GCOP, they are failing to meet their duty to indemnify insureds for a necessary cost of restoring insured assets to pre-loss condition. Improper exclusion of GCOP by insurance companies creates shortfalls in repair and rebuilding financing for property owners *and* negatively impacts the local, state and federal government entities that have an interest in communities' successful economic recovery and the restoration of property tax bases. UP's library of publications, tools and guidance includes many publications addressing GCOP. *See, e.g.* "Full and fair insurance payouts foster safe and sound construction" at <https://www.uphelp.org/blog/full-fair-insurance-payouts-foster-safe-and-sound-construction>

and-fair-insurance-payouts-foster-safe-and-sound-construction; and “What’s UP with Overhead and Profit?” at [https://www.uphelp.org/pubs/what%E2%80%99s-overhead-and-profit#\\_ftnref2](https://www.uphelp.org/pubs/what%E2%80%99s-overhead-and-profit#_ftnref2).

A diverse range of policyholders throughout the U.S. regularly communicate their insurance concerns to UP, which allows UP to submit informed *amicus curiae* briefs to assist state and federal courts in cases involving important insurance principles. UP has filed *amicus curiae* briefs in approximately 450 cases throughout the United States. UP’s *amicus curiae* brief was cited in the United States Supreme Court’s opinion in *Humana, Inc. v. Forsyth*, 525 U.S. 299 (1999) and arguments from UP’s *amicus curiae* brief have been cited with approval by numerous state and federal appellate courts. See: <https://www.uphelp.org/resources/amicus-briefs>.

UP seeks to fulfill the “classic role of *amicus curiae* by assisting in a case of general public interest, supplementing the efforts of counsel, and drawing the court’s attention to law that escaped consideration.” *Miller-Wohl Co., Inc. v. Comm’r. of Labor & Indus.*, 694 F.2d 203, 204 (8th Cir. 1982).

## **II. SUMMARY OF ARGUMENT**

Property insurance provides financial security for homeowners and businesses. The question at issue may seem esoteric: whether general contractor overhead and profit (“GCOP”) can be excluded when an insurance company pays actual cash value (“ACV”) benefits under property insurance policies affording replacement cost coverage. But in practice, ensuring that GCOP is paid with an ACV settlement is critical for ensuring that policyholders receive the full benefit of their coverage. The Superior Court erred in reversing the trial court’s ruling that Pennsylvania law requires GCOP to be included in ACV settlements.

Here, Truck Insurance Exchange (“Truck”) “determined that the services of a general contractor would likely be necessary to repair the value of the property.” (Superior Court Mem. Op. at 5). Nevertheless, Truck excluded GCOP in its calculation of the ACV settlement. (*Id.*) Truck cited language its policies authorizing it to withhold GCOP from ACV payments “unless and until you actually incur and pay such fees and charges, **unless the law of your state requires that such fees and charges be paid with the actual cash value settlement.**” (emphasis added). The Superior Court below acknowledged that existing Superior Court precedent, *Gilderman v. State Farm Insurance Company*, 649 A.2d 941 (Pa. Super. 1994), held that GCOP must be included within “actual

cash value,” as actual cash value means the actual cost of repair or replacement less depreciation. GCOP is part of replacement cost and does not depreciate, so it is within ACV and is required to be paid as part of the ACV settlement under Pennsylvania law.

The Truck policy explicitly defines “actual cash value” in exactly the way the Superior Court defined the term “actual cash value” in *Gilderman* where State Farm had left the term undefined. From an interpretive perspective, the initial question becomes simple: Does *Gilderman* state “the law of” Pennsylvania that requires GCOP to be paid with the ACV settlement; or would it be so only if, as the Superior Court assumed, the court in *Gilderman* had ruled that “public policy” required that ACV include GCOP? In our view, the answer is simple. Pennsylvania law requires GCOP to be paid with an ACV settlement because, under Pennsylvania law, GCOP is part of ACV, which includes any cost that an insured is reasonably likely to incur in repairing or replacing a covered loss, minus depreciation, and GCOP does not depreciate.

For good reason, courts interpret ambiguities in insurance policies in favor of finding coverage for the policyholder. Insurance policies are often contracts of adhesion, drafted not jointly, but by one party with vastly more economic power. In addition, insurance contracts are aleatory contracts; the policyholder pays

premium up front and the insurance company performs later only if an uncertain event occurs. Because the insurance company has already received performance from the policyholder (payment of premium), there can be an incentive to breach when the insurance company is later called upon to perform. Moreover, the fundamental purpose of insurance is to insure, so doubts in language should be resolved to fulfill the essential contractual purpose of the insurance transaction and the reasonable expectations of the insurance consumer.

In addition to the interpretative question, there is the public policy question raised but not decided by the Superior Court: Does Pennsylvania public policy require that ACV settlements include GCOP? The Superior Court noted only that the plaintiffs had “not identified any case that sets forth a public policy that actual cash settlement value must include GCOP.” (Superior Court Mem. Op. at 9). If this court decides that the interpretive question does not resolve the matter in favor of coverage, this Court can and should recognize such a public policy, as it is in accord with existing Pennsylvania precedent (*Gilderman*) and the established customs and practices of the insurance industry. The holdback of GCOP results in policyholders not receiving the full ACV and, due to a lack of resources, it can result in policyholders never being able to access the replacement cost benefits for which they have paid an additional premium.

### **III. STATEMENT OF FACTS**

The parties are addressing the particular facts of this case, so UP will not repeat them here. Determining whether GCOP should be included in the ACV adjustment of a property insurance claim depends on the understanding of unique property insurance concepts and coverages, such as those contained in the Appellants' policies. Therefore, to assist the court, we provide a brief tutorial on some of the key insurance terms.

#### **Actual cash value**

Generally, ACV is the amount required to put a policyholder back to where he or she was before the loss. "Actual cash value of property may be paraphrased as: ITS WORTH IN MONEY AT THE PRESENT MOMENT." National Committee on Property Insurance, *Actual Cash Value Guidelines: Buildings, Personal Property*, 5 (1982) (emphasis in original). 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 corollary to this principle is that the ACV approach should

never be employed to underpay a claim by providing less than indemnity. ACV is “replacement cost minus any depreciation (i.e. wear and tear).”<sup>1</sup>

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 not destroyed by hail. Disputes arise 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 before the loss. Historically, insurance companies did not define ACV, but here the policy defines ACV as replacement cost less depreciation. As such, an understanding of what constitutes “replacement cost” is significant.

### **Replacement Cost**

Replacement cost or replacement value is the cost to replace lost or damaged property with new property of comparable quality, at current market value, up to the policy limits. “Replacement cost coverage reimburses an insured for the full cost of repairs, if she repairs or rebuilds the building, even if that results in putting the insured in a better position than she was in before the loss.” 5-47 New

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<sup>1</sup> See “Homeowners Insurance Guide,” Pennsylvania Insurance Department at <https://www.insurance.pa.gov/Coverage/Documents/Homeowners/Homeowners%20Insurance%20Guide.pdf>.

Appleman on Ins. Law Library Ed. §47.04[2][b] (2016). “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, Insurance Claims and Disputes § 11:35 (6<sup>th</sup> ed., March 2018 Update) (emphasis added).

Replacement cost coverage is a relatively modern concept in insurance because it exceeds the traditional concept of indemnity, which is to return the insured to the financial position occupied immediately before the loss occurred. The insured will arguably be in a better place financially when older property is replaced with new, but policyholders pay a higher premium for this coverage. 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.

The timing of ACV and replacement cost payments can differ. An insurance company may elect to pay ACV as soon as it determines the replacement cost and depreciation, holding back the depreciation until the policyholder actually repairs or replaces the property. The policy may even put a time limit, sometimes as short as 180 days after payment of the ACV, on when the policyholder must repair or

replace the property in order to receive the full replacement costs. *See Sher v. Allstate Ins. Co.*, 947 F.Supp.2d 370 (S.D.N.Y. 2013). When an insurance company retains amounts for GCOP and pays less in ACV coverage, the policyholder may not have enough funds to rebuild the damaged property within the required time period. In that instance, the coverage could be forfeited and the insurance company *never pays* the replacement cost coverage for which the policyholders contracted and paid.

### **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.’” 5-47 New Appleman on Ins. Law Library Ed. §47.04[2][a] (2016); *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; it has depreciated in value.

### **Overhead and profit**

Overhead and profit are costs included in repair estimates. Specifically, overhead includes “fixed costs to run the contractor’s business, such as salaries, rent, utilities, and licenses,” and profit “is the amount the contractor expects to earn for his services.” *Trinidad v. Fla. Peninsula Ins. Co.*, 99 So. 3d 502, 502-03 (Fla. 3d DCA 2011).

## **IV. ARGUMENT**

### **A. The Law of Pennsylvania Requires That GCOP Be Paid With the Actual Cash Value Settlement.**

The policy issued by Truck to Appellants is a replacement cost policy for which Appellants paid an additional premium. The Truck policy has a two-step payment process. Truck is required to pay the ACV necessary to repair the damaged property, withholding a deduction for depreciation until the repairs have been completed. The policy defines “Actual Cash Value” as “the reasonable replacement costs at the time of loss less depreciation for both economic and functional obsolescence.” The term “replacement costs” is not defined in the Truck policy, but that is of no moment because it is undisputed that GCOP is properly part of the reasonable replacement costs at the time of loss. Obviously, GCOP is not subject to depreciation for either economic or functional

obsolescence. Therefore, GCOP is within the plain meaning of ACV under the Truck policy.

The policy also includes a “How We Settle Covered Loss” in part:

(3) . . . However, **actual cash value** settlements will not include estimated general contractor fees or charges for general contractor’s services unless and until you actual incur and pay such fees and charges, **unless the law of your State requires that such fees and charges be paid with the actual cash value settlement.**

(Emphasis added). Accordingly, under the policy language, while GCOP is part of the definition of “actual cash value” in the Truck policy, it need not be paid as part of an ACV settlement unless and until GCOP is paid **unless** the law of Pennsylvania requires that GCOP be paid with the ACV settlement.

Pennsylvania law has long required insurance companies to pay GCOP as part of an ACV settlement. In the 1994 case of *Gilderman v. State Farm Insurance Company*, 659 A.2d 941 (Pa. Super. 1994), the insured had a replacement cost policy, but was to receive ACV before any repairs or replacement. The policy limited recovery to the amount actually incurred in repairing or replacing the damaged property. *Id.* at 942–43. The appellate court considered whether State Farm could deduct GCOP from its repair or replacement estimate and offer the insureds an advance check for this lower amount as a payment of ACV. *Id.* at 944. In rejecting State Farm’s position, the court noted “there are types of property

damage where a homeowner would use the services of a general contractor[,] ... especially where there is extensive damage to a home requiring the use of more than one trade specialist.” *Id.* The court found that, in these instances, an insurance company may not deduct contractor fees from the ACV when such fees are reasonably expected to occur. *Id.* The court extended this rationale to instances when the insured might not actually incur labor costs, i.e., when the insured makes his or her own repairs to a covered loss. *See id.* Thus, the court found State Farm’s automatic deduction of contractor fees improper, holding that “repair or replacement costs include any cost that an insured is reasonably likely to incur in repairing or replacing a covered loss,” even if the insured may never make the repairs. *Id.*

As further explained in *Mee v. Safeco Insurance Company of America*, 908 A.2d 344 (Pa. Super. 2006), the law of Pennsylvania provides that the actual cash value to be paid by a property insurance company includes all repair and replacement costs (including GCOP), minus depreciation:

From *Gilderman*, we take the following legal principles: (1) actual cash value includes repair and replacement costs; (2) repair and replacement costs include O & P where use of a general contractor would be reasonably likely; (3) because a homeowner pays higher premiums for repair and replacement coverage, he is entitled to O & P where use of a general contractor would be reasonably likely, even if no contractor is used or no repairs are made.

*Mee*, 908 A.2d at 350 (footnote omitted). The quoted discussion of *Gilderman* in *Mee* is a succinct summary of Pennsylvania law on the issue.

Here, Judge Djerassi in the Court of Common Pleas applied Pennsylvania law and properly found:

The approach taken in *Gilderman* and *Mee* is the law today. Insurance companies are required in Pennsylvania to include general contractor overhead and profit in Actual Cash Value payments for losses where repairs would be reasonably likely to require a general contractor. *Gilderman* and *Mee* would reflect the majority of approach across jurisdictions.

(Superior Court Mem. Op. at 11). Accordingly, Judge Djerassi recognized that Pennsylvania law requires that GCOP be paid with an ACV settlement.

Other jurisdictions have adopted the reasoning in *Gilderman* and have ruled that an insurance company may not deduct a contractor's overhead and profit from an ACV payment. *See Mills v. Foremost Ins. Co.*, 511 F.3d 1300, 1305 (11th Cir. 2008) ("[The insureds] contracted for the [ACV] of their loss and their recovery is not tied to actually making the repair or replacement."); *Parkway Assocs., LLC v. Harleysville Mut. Ins. Co.*, 129 F.App'x 955, 962-63 (6th Cir. 2005) ("[ACV] is not calculated based upon what the insured ultimately pays to repair her property"); *Mazzocki v. State Farm Fire & Casualty Corp.*, 1 A.D.3d 9, 766 N.Y.S.2d 719, 722 (2003) (an insurer was "obligated to include profit and overhead in ... [ACV], whenever a general contractor would likely be needed.");

*Ghoman v. New Hampshire Insurance Co.*, 159 F.Supp.2d 928, 934 (N.D. Tex. 2001) (a contractor's overhead and profit fees constituted “any cost that an insured is reasonably likely to incur in repairing or replacing a covered loss” and, thus, should be included in the ACV payment.); *Bankers Sec. Ins. Co. v. Brady*, 765 So.2d 870, 872 (Fla. 5<sup>th</sup> DCA 2000) (stating in dictum that, because insurer paid insured before repair or replacement, insurer could not withhold overhead and profit); *Weidman v. Erie Ins. Group*, 745 N.E.2d 292, 298 (Ind. Ct. App. 2001) (where ACV of loss was set by appraisal, and insurance policy had no provision authorizing insurer to later withhold contractor fees when insured completed own repairs).

Thus, the plain meaning of the policy supports the Court of Common Pleas' ruling that Truck may not withhold GCOP from an ACV settlement because Pennsylvania law requires it to be included. A simple example shows that not including GCOP in an ACV settlement is fundamentally unfair and unreasonable under the policy language at issue. Imagine a situation where there has been no depreciation; for example, when a brand new home is destroyed by fire the day after a homeowner moves in. The replacement cost indisputably includes GCOP. The ACV should equal the replacement cost in this scenario because, as the example assumes, there has been no depreciation and the policy defines ACV as

“the reasonable replacement costs at the time of loss less depreciation for both economic and functional obsolescence.” Under Truck’s interpretation, however, Truck could pay less for an ACV settlement than for a replacement cost settlement because it could withhold GCOP. That is not a reasonable interpretation of the policy language.

**B. Public Policy Requires That GCOP Be Paid With the Actual Cash Value Settlement.**

Several state departments of insurance across the country have condemned insurance company efforts to deduct GCOP from replacement cost when calculating ACV. They are important indicia of the standards and practices of the insurance industry. They show that industry usage of the term ACV includes GCOP and that it is improper for an insurance company to withhold GCOP from an ACV settlement. This is in accord with the law and public policy of Pennsylvania.

The Colorado Division of Insurance recently confirmed it would not be repealing a longstanding insurance bulletin requiring that GCOP be part of a calculation to determine ACV in residential insurance policies.<sup>2</sup>

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<sup>2</sup> See “Notice of Stakeholder Meeting on Bulletin 5.1” at <https://content.govdelivery.com/accounts/CODORA/bulletins/24532eb>.

The Colorado bulletin provides, in part:

**Insurers shall be prohibited from deducting contractors' overhead and profit** in addition to depreciation when policyholders do not repair or replace the structure.

...

The position of the Division of Insurance is that the actual cash value of a structure under a replacement cost policy, when the policyholder does not repair or replace the structure, is the full replacement cost with proper deduction for depreciation. **Deduction of contractors' overhead and profit, in addition to depreciation, is not consistent with the definition of actual cash value.** The Division of Insurance will interpret policy provisions containing the foregoing or similar language to prohibit deduction of contractors' overhead and profit, in the calculation of actual cash value, where the dwelling is not repaired or replaced by the policyholder.

*See Bulletin B-5.1, Calculation of actual cash value: Prohibition against deducting contractors' overhead and profit from replacement cost where repairs are not made.* (emphasis added).

Other state insurance departments have issued similar bulletins. In 1992, Florida published an insurance bulletin prohibiting the withholding of overhead and profit, stating in part:

This authority is specifically applicable to the practice by insurers of imposing a “holdback” of insurance proceeds greater than actual cash value until replacement has taken place. While this practice is appropriate for personal property, this bulletin serves to place insurers on notice that for partial losses on real property, the “holdback” is inconsistent with established precedent.

The application of a “holdback” to repair of real property can particularly cause hardship to the insured when the actual cash value payment is insufficient to enter into a contract to make repairs. In such an instance, the insured may be forced to seek other funding sources, at his expense, in order to contract for repairs.

Insurers who have been applying “holdbacks” in claims for partial loss on real property should pay the actual amount of the loss. The best indicator of actual loss is the contract for repair entered into by the insured. Once an actual amount of loss is determined by contract, the full loss payment should be made with no hold back applied. This arrangement satisfies the public policy interests both in timely and sufficient claim payments, and in encouraging rebuilding. In instances where a holdback is currently being applied and a repair contract has been executed, the holdback should be released.

Florida Department of Insurance Informational Bulletin No. 92-036, (December 8, 1992). On June 12, 1998, the Texas Insurance Commissioner issued a bulletin, very similar to the one in effect in Colorado, which provides in part:

Indemnity is the basis and foundation of insurance coverage. The objective is that the insured should neither reap economic gain nor incur a loss if adequately insured. This objective requires that the insured receive a payment equal to that of the covered loss so that the insured will be restored to the same position after the loss as before the loss. The calculation of this payment results in under-compensation if an insurer deducts prospective contractors' overhead and profit and sales tax in determining the actual cash value under a replacement cost policy. Conversely, the inclusion of contractor's overhead and profit and sales tax on building materials does not over-compensate an insured for the amount of the loss because these items represent part of the insured's loss. Generally, the objectives of indemnity will be met if actual cash value is calculated as replacement cost with proper deduction for depreciation. In the rare situation that defies calculation of actual cash value on this basis, such as cases in which the structure has historical significance or the materials cannot

reasonably be replaced, other factors may be considered. However, there is no situation in which the deduction from replacement cost of depreciation and contractor's overhead and profit and/or sales tax on materials will be the correct measure of the insured's loss.

...

*To deduct costs other than depreciation from the estimated replacement cost of the damaged structure is contrary to historical industry norms and practices.* Historically, insurers have determined actual cash value on the basis of repair or replacement cost less depreciation. Only recently have some insurers deducted contractor's overhead and profit and sales taxes on building materials. There has been no recent change in the language in the promulgated residential property policies to support such a change in determining actual cash value.

The insurers' argument that the cost of contractor's overhead and profit and sales tax on building materials should be excluded from an actual cash value loss settlement because the insured has not incurred these expenses is not persuasive. Using this logic, an insured who opts not to repair or replace damaged property would not incur any of the expenses necessary to repair or replace the damaged property, including the costs of building materials, and would collect nothing under an actual cash value loss settlement. This result would be contrary to the purposes of the subject insurance policy.

Texas Department of Insurance, Commissioner's Bulletin No. B-0045-98, <http://www.tdi.texas.gov/bulletins/1998/b-0045-8.html>. (emphasis added.) This 1998 Bulletin was reaffirmed as the proper method of property insurance again in 2008. Texas Department of Insurance, Commissioner's Bulletin No. B-0068-08, <https://tdi.texas.gov/bulletins/2008/cc70.html>.

### **C. Industry Custom and Practice Has Consistently Included GCOP in ACV Settlements.**

This Court has instructed that “[w]herever reasonable, the manifestations of intention of the parties to a promise or agreement are interpreted as consistent with each other and with any relevant course of performance, course of dealing, or usage of trade.” *Sunbeam Corp. v. Liberty Mut. Ins. Co.*, 566 Pa. 494, 501, 781 A.2d 1189, 1193 (2001) (quoting Restatement (Second) of Contracts § 202(5)).

The interaction of GCOP with ACV and replacement cost calculations is well established in the insurance industry, and the usage of those terms in the insurance trade confirms that GCOP is included in ACV. In addition to the insurance department bulletins previously referenced, commonly used insurance industry textbooks include GCOP as a component of repair or replacement cost that is not held back or subject to depreciation when making an ACV settlement.

Recovery of GCOP as part of an ACV settlement is an accepted standard and practice in the industry. This was discussed in an *Adjusting Today* article titled “Overhead and Profit: Its Place in a Property Insurance Claim”:

The Property Law Research Bureau (“PLRB”), a recognized resource used by insurers in the interpretation of property insurance policy provisions has taken the position “contractor’s overhead and profit are included in ACV, because they are part of replacement costs.”

Edward Eshoo, Jr., *Adjusting Today: “Overhead and Profit: Its Place in a Property Insurance Claim,”* 5 (October 11, 2007). PLRB concludes that “any estimate of actual cash value should include overhead and profit.” *See, id.*, at 6.<sup>3</sup>

The National Underwriter Company publishes under the name Insurance Coverage Law Center (“ICLC”), formerly FC&S, or Fire, Casualty & Surety, a comprehensive library of reference books for insurance professionals. The ICLC also provides online bulletins in which its experts respond to questions from insurance professionals. These bulletins are used by insurance agents and brokers to interpret standard insurance policy provisions. The ICLC addressed its position that contractor’s overhead and profit, in addition to depreciation, should not be deducted from an ACV settlement:

. . . Contractors’ overhead and profit is included in arriving at a replacement cost figure. Actual cash value is determined by deducting depreciation from the replacement cost figure. The insurer in [Gilderman et al. v. State Farm Ins. Co., 649 A.2d 941 (Pennsylvania 1994)] attempted to deduct depreciation and an additional amount representing contractors’ overhead and profit. The court, quite rightly, disagreed with this procedure.

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<sup>3</sup> *Property Loss Adjusting* is a textbook for property claims adjusters published by the Insurance Institute of America for its industry-wide insurance designation and certification programs. It lists several elements as comprising repair or replacement cost: materials, labor and employers’ burden, tools and equipment, overhead and profit and miscellaneous direct costs such as permits and taxes. Markham, James. J., *Property Loss Adjusting*, Vol. II, at pp. 5-9.

ICLC Bulletin, *Actual Cash Value and Total Fire Loss* (Nat'l Underwriter Co. November 4, 2009). Likewise, former insurance company attorney and frequent expert witness for insurance companies Barry Zalma explains that “[t]here is no basis for simply withholding profit and overhead as a means of calculating actual cash value.” Barry Zalma, *Representing Insureds in a Catastrophe*, 41 Tort Trial & Ins. Prac. L.J. 817, 840 (2006) (emphasis added).

As these authorities recognize, excluding the payment of GCOP would not effectuate the purpose of ACV coverage, which is indemnity, *i.e.*, placing policyholders back in the position they enjoyed before the loss.<sup>4</sup> Of course, ACV coverage can never put the policyholders back in the *precise* position they were in before the loss because if a ten-year old roof is destroyed the only way to return the policyholders back to the exact position they were in before the loss would be to

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<sup>4</sup> Here, Truck’s interpretation of the policy under Pennsylvania law provides less coverage than what is contained in the 1943 New York Standard Fire Insurance Policy (“Standard Fire Insurance Policy”), a 165-line form providing coverage for direct loss by fire and lightning, which is used in many states. In Pennsylvania, the statutorily mandated language that must be included in every Standard Fire Insurance Policy is contained in 40 Pa. C.S.A. section 636. That language requires that the measure of an insured’s loss be “actual cash value.” The rule in Pennsylvania regarding actual cash value coverage “seeks a result which will enable the parties to restore the property to as near the same condition as it was at the time of the fire, or pay for it in cash.” *Fedas v. Insurance Co. of Pennsylvania*, 300 Pa. 555, 563-64, 151 A. 285, 288 (Pa. 1930). Thus, Truck’s withholding GCOP from Appellants’ ACV payment frustrates the purpose of indemnity.

install a ten-year old roof. That is not feasible as you cannot buy and install a used roof, or used roofing material. Therefore, ACV provides a policyholder the cost of a new roof, minus the amount that the roof has deteriorated. Before the loss, the insureds had a ten-year old roof installed on the house. To be made whole, the insurance company 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 GCOP is the same. Another simple example shows how unfair it would be to allow insurance companies, such as Truck, to withhold GCOP from an ACV settlement:

A retired pilot saves his money for a retirement home and builds it on land he has long owned in Lancaster. The home is built for the cost of \$1,000,000. He buys replacement cost insurance for \$1,000,000. Two days after the construction is complete, a jet which ran out of fuel crashes into the home, destroys it and a guest of his in the house died. The retired pilot makes a claim for \$1,000,000 — the cost to rebuild the structure. The insurance company says it does not have to pay the general contractor overhead and profit until he rebuilds the house. So, they deduct the approximate 20% amount per the estimate and pay him \$800,000 as the replacement cost less the contractor's overhead and profit. To add insult to injury, the retired pilot decides he never wants to rebuild at the site because of the emotional incident. In summary, he just paid \$1,000,000 for the house, bought insurance for \$1,000,000 and the insurance company will only pay an amount less than the agreed replacement cost.

Withholding GCOP prevents making the policyholder whole and frustrates the indemnity purpose of ACV coverage<sup>5</sup>.

**D. The Law of Pennsylvania Requiring Insurance Policies To Be Interpreted In Favor of Coverage Is Well Supported By Public Policy and Precedent.**

If there is any ambiguity in the policy language, that ambiguity must be resolved in favor of the policyholder Appellants. This Court has long held that when multiple reasonable interpretations of an insurance policy are possible, the language must be read in favor of coverage. *See, e.g., Prudential Prop. & Cas. Ins. Co. v. Sartno*, 903 A.2d 1170, 1177 (Pa. 2006). This Court's precedent is

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<sup>5</sup> Truck's position of withholding GCOP as part of an ACV settlement may also render coverage potentially illusory, as explained in the example *supra*, at 23. *See also Jostens, Inc. v. Northfield Ins. Co.*, 527 N.W.2d 116, 118 (Minn. Ct. App. 1995) (the doctrine of illusory coverage is "an independent means to avoid an unreasonable result when a literal reading of a policy unfairly denies coverage."). Further, a policy that requires an insured to pay an extra sum for replacement cost coverage and, in return for the extra sum, fails to provide the insured with the benefits the insured would expect from an ACV policy unreasonably favors the insurance carrier and is therefore unconscionable. *See Standard Venetian Blind Co. v. American Empire Ins. Co.*, 503 Pa. 307, 469 A.2d 566 (1983) ("A court may refuse to enforce a contract or any clause of contract if [the] court as a matter of law deems the contract or any clause of the contract to be unconscionable at the time it was made."). *See Koval v. Liberty Mutual Insurance Company*, 366 Pa.Super. 423-24, 531 A.2d 491 (1987) (explaining Pennsylvania's two-prong test in determining unconscionability: first, one of the parties must have lacked a meaningful choice whether to accept the provision and, second, the provision must unreasonably favor the other party to the contract.)

uniformly adopted across the country. It is critical to the enforcement of insurance policies, which are imbued with the public interest.

As explained in an article written by Professor Henderson of the University of Arizona College of Law:

[T]he insurance industry plays a very important institutional role by providing the level of predictability requisite for the planning and execution that leads to further development. Without effective planning and execution, a society cannot progress.

....

Insurance is purchased routinely and has become pervasive in our society. It protects against losses that otherwise would disrupt our lives, individually and collectively. The public interest, as well as the individual interests of millions of insureds, is at stake. This is the foundation for the general judicial conclusion that the business of insurance is cloaked with a public purpose or interest.

Roger C. Henderson, *The Tort of Bad Faith in First-Party Insurance Transaction: Refining the Standard of Culpability and Reformulating the Remedies By Statute*, 26 U. of Mich. J. L. Ref. 1, 9-11 (Fall 1992) (footnotes omitted).

The field of insurance differs from any other business involving commercial contracts, based on its high degree of interaction with a potentially vulnerable portion of the consuming public. As explained in an insurance industry treatise, *The Legal Environment of Insurance* in its chapters on Insurance Contract Law:

The insurance contract has the same basic requisites as other contracts. There is a need for an agreement, competent parties, consideration, and a legal purpose. However, the insurance contract also has other distinctive features. Insurance contracts cover fortuitous events, are contracts of adhesion and indemnity, must have the public interest in mind, require the utmost good faith, are executory and conditional, and must honor reasonable expectations.

James J. Lorimer, et al, *The Legal Environment of Insurance* 176 (American Institute for Charter Property Casualty Underwriter, 4th ed. 1993).

Insurance is far from the market ideals of complete information and no transaction costs. Opportunistic breaches are especially likely because of the aleatory nature of those contracts, with the insurance company's performance coming long after the policyholder has performed. *See* Mark Pennington, *Punitive Damages for Breach of Contract: A Core Sample from the Decisions of the Last Ten Years*, 42 ARK. L. REV. 31, 54 (1989); *see also* *Communale v. Traders & Gen. Ins. Co.*, 328 P.2d 198, 200-02 (Cal. 1958). Thus, insurance is special:

Insureds bought insurance to avoid the possibility of unaffordable losses, but all too often they found themselves embroiled in an argument over that very possibility. . .

. . . Insureds did not plan for litigation as an institutional litigant would. Insurers, on the other hand, built the anticipated costs of litigation into the premium rate structure. In effect, insureds, by paying premiums, financed the insurers' ability to resist claims. Insureds,

as a group, were therefore peculiarly vulnerable to insurers who, as a group, were inclined to pay nothing if they could get away with it, and, in any event, to pay as little as possible. Insurance had become big business.

Roger C. Henderson, *supra* at 13-14.

Against this background, to protect policyholders and create consistency, comprehensive rules of policy interpretation have developed. They boil down to this:

[w]hen interpreting insurance policies, as a matter of public policy, ambiguities are generally construed in favor of the insured and against the insurer. Thus, where the policy is found to be unclear and ambiguous, the court's construction of an insurance policy will be guided by the reasonable expectations of the insured.

*Ponder v. State Farm Mut. Auto. Ins. Co.*, 12 P.3d 960, 967 (N.M. 2000) (internal quotation omitted); *see also Gen. Cas. Co. of Wis. v. Hills*, 561 N.W.2d 718, 722 (Wis. 1997) (“[o]f primary importance is that the language of an insurance policy should be interpreted to mean what a reasonable person in the position of the insured would have understood the words to mean”).

The ambiguity doctrine has deep roots. In *American Surety Co. of N.Y. v. Pauly*, 170 U.S. 133, 144 (1898), the United States Supreme Court held that ambiguities in insurance policy language must be construed against the insurance company, because (even then) the ambiguity doctrine was “a well established rule

in the law of insurance.” As explained and applied by this Court, any reasonable interpretation of insurance policy language favoring the policyholder should be adopted, even if there are other reasonable interpretations. *Prudential Prop. & Cas. Ins. Co. v. Sartno*, 903 A.2d 1170, 1177 (Pa. 2006). As the party who selects the language used in the insurance policy, the insurance company must be clear and specific in its use. *Sartno*, 903 A.2d at 1178. *See also Safran v. Mut. Life Ins. Co. of New York*, 210 Pa. Super. 408, 413, 234 A.2d 1, 4 (1967) (Pennsylvania courts adhere to the rule of liberal construction in construing insurance contracts); *Limandri v. Allstate Ins. Co.*, No. CV 16-2960, 2019 WL 1429666 (E.D. Pa. Mar. 29, 2019) (when a provision in an insurance policy is ambiguous under Pennsylvania law, the policy should be construed in favor of the insured to further the contract’s prime purpose of indemnification, as the insurer drafts the policy, and controls coverage); *Toffler Assocs., Inc. v. Hartford Fire Ins. Co.*, 651 F. Supp. 2d 332, 343 (E.D. Pa. 2009) (the test to be applied in determining whether there is an ambiguity in a policy is not what the insurer intended it to mean, but what a reasonable person in the position of an insured would understand the words to mean).

## **V. CONCLUSION**

UP recognizes and appreciates the extremely important role insurance plays in modern society. Profitable and financially stable insurance companies promote a healthy society, allowing risks of loss to be spread widely and fairly. When the system works, prompt and proper payment goes to those who suffer life-altering catastrophes affecting their persons and property. The inclusion of GCOP in ACV payments is a well-established and important standard and practice in the insurance industry. Pennsylvania courts and various insurance commissioners have all acknowledged that GCOP is properly a part of an ACV settlement. UP respectfully requests that the Court reverse the decision of the panel of the Superior Court and find that GCOP is owed under the Truck policy as part of an ACV settlement in Pennsylvania.

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Respectfully submitted,

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## **CERTIFICATE OF COMPLIANCE**

Pursuant to Pennsylvania Rules of Appellate Procedure 531 and 2135, the length of this amicus curiae brief is 6,736 words, in compliance with the word count limit of 7,000 words.

/s/ William F. Merlin, Jr.  
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## **PROOF OF SERVICE**

I hereby certify that I am this day serving the foregoing document upon the persons listed below via the PACFile system, which service satisfies the requirements of Pa.R.A.P. 121. To the extent the PACFile system is unable to serve any of the persons listed below, such persons will be served via first class U.S. Mail.

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## **ADDENDUM**

1. Edward Eshoo, Jr., *Adjusting Today: “Overhead and Profit: Its Place in a Property Insurance Claim”* (October 11, 2007)
2. Florida Department of Insurance Informational Bulletin No. 92-036, (December 8, 1992)
3. National Committee on Property Insurance, *Actual Cash Value Guidelines: Buildings, Personal Property* (1982)