Diminished Value:

Kicking the Chihuahua

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Automobile diminished value cases are like Chihuahuas. When you first see one, it just does not look right. It is small and annoying, and should not be recognized as a breed of dog. However, if you kick at it, it is likely to bite you on the ankle.

The Chihuahua in Georgia

Recently in Georgia, State Farm tried to kick the Chihuahua, apparently thinking it was small and insignificant. However, as a result, the Georgia Supreme Court bared its teeth on all Georgia insurers. The case at issue, *State Farm Mutual Automobile Insurance Co. v. Mabry*, 274 Ga 498, 556 SE 2d 114 (2001), definitively established the right of Georgia insureds to obtain compensation for first-party diminished value claims.

Diminished value in the automobile setting is the difference between the value of a vehicle prior to an accident and the value of the vehicle after an accident, even where repairs have been made. Put more simply, if two vehicles are placed side by side, and they are identical with the exception that one had sustained damage and was repaired, the diminished value would be the difference in the price each vehicle would fetch in the market place. The insured typically argues that a consumer would not be willing to pay as much for a vehicle that has been damaged and repaired as one that has never been damaged.

Mabry addressed diminished value of automobiles under a first-party claim and looked at whether an insurer had an obligation to pay diminished value to its insured pursuant to the terms of the policy. The lawsuit obtained certification as a class action with a class that included "all current insureds under State Farm policies issued in Georgia." 274 Ga at 498. The Georgia Supreme Court ultimately held that not only could an insured recover diminished value, but that the Georgia Insurance Commission had an affirmative duty to impose regulations on the insurance companies requir-

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ing it to devise methods by which to evaluate the diminished value claims of their insureds. As a result, insurers in Georgia now must evaluate diminished value as a matter of course when handling a first-party motor vehicle property damage claim.

The issue of diminished value in a first-party claim is raised by an action for breach of the insurance contract. As such, the language of the insurance contract will govern the outcome. In reaching its decision recognizing first-party claims for diminished value, *Mabry* looked to the language in the State Farm auto policy, which stated "State Farm will 'pay for loss to your car,' minus any deductible." *Id* at 502 (quoting the State Farm policy). State Farm's obligation under the policy, therefore, was to pay either the actual cash value of the vehicle or the cost of repair or replacement. State Farm had the option to settle the claim for payment up to the cash value of the vehicle or payment "to repair or replace the property or part with like kind and quality." *Id.*

A battle began between plaintiffs and State Farm as to what constituted the value of the "loss to your car." Plaintiffs contended in order to be fully compensated for their loss, they must be paid the difference between the pre-accident value of the vehicle and the post-accident value of the vehicle and that the difference in value had to include the diminished value. State Farm contended if the vehicle was repaired satisfactorily, there would be no diminished value. However, State Farm's own evidence fairly well established that if a vehicle has been in an accident, regardless of the quality of the repairs, people would tend to pay less for it than they would pay for a like kind vehicle that had not been in an accident. State Farm argued in the alternative that if there were diminished value, plaintiffs would not realize the loss until the vehicle was sold. This is an argument insurance companies frequently make, since the insured has not truly realized a financial loss where he or she retains the vehicle.

The ruling required State Farm to develop procedures to evaluate claims to determine if diminished value existed and to collect, catalog, and maintain information needed to evaluate diminished value.

The court turned to the issue of interpreting the insurance contract to determine whether the contract required State Farm to pay diminished value. The court analyzed a long line of Georgia cases in which the term "repair" as used in the insurance policy was interpreted as meaning "restoration of the vehicle to substantially the same *'condition and value* as existed before the damage occurred.'" Thus, to restore the vehicle to pre-accident value, the insured had to be compensated for the diminished value of the vehicle.

The Georgia Supreme Court went one step further because of a claim by plaintiffs for injunctive relief and upheld the trial court's order requiring State Farm to establish a method by which to evaluate diminished value claims. The ruling required State Farm to develop procedures to evaluate claims to determine if diminished value existed and to collect, catalog, and maintain information needed to evaluate diminished value.

That Dog Don't Hunt: Alabama and California Holdings

More recently, the Alabama Civil Appeals Court, hearing virtually identical arguments as had been made in *Mabry*, came to the opposite conclusion, finding Alabama law did not support a first-party claim for diminished value. The Alabama decision came in the form of another class action suit against State Farm called *Pritchett v. State Farm Mutual Automobile Ins. Co.*, Ala Civ App No. 2000850 (February 22, 2002). In *Pritchett*, the Alabama appeals court, on a case of first impression, held that given the plain meaning of the policy language, State Farm was responsible for paying either the cash value of the vehicle or paying for repairs.

Again the decision came down to the interpretation of the word "repair" as contained in the policy. In interpreting the word "repair," the Alabama court looked to Black's Law Dictionary and other dictionaries and determined they defined the word "repair" as a restoration of the physical condition of a damaged item and not as a restoration of the value of an item. Therefore, because the term "repair" had no connection to value, but rather to physical condition, the obligation of the insurer to repair the vehicle was an obligation to restore the vehicle to its pre-accident physical condition and not an obligation to compensate the insured for the diminished value of the vehicle.

In 1988, California also held diminished value was not recoverable under a

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first-party breach of contract claim against an insurer. In *Ray v. Farmers Insurance Exchange*, 200 Cal App 3d 1411, 246 Cal Rptr 593 (1988), the California Court of Appeals held that language in the Farmers' policy that it would pay either the "actual cash value" or repair or replace the vehicle with "like kind and quality" demonstrated that Farmers recognized the distinction between the concepts of value and vehicle condition. The court refused to impose on Farmers the obligation of insuring the actual cash value of the vehicle in situations where Farmers elected to repair the vehicle, since to do so would defeat the ability of Farmers to elect the remedy, as provided for by the policy.

To Kick or Not: Oregon

Oregon has little case law on the issue of diminished value in motor vehicle claims. In first-party diminished value claims, Oregon's case law starts and stops in 1941 with the case of *Dunmire Motor Co. v. Oregon Mutual Fire Ins. Co.*, 166 Or 690, 114 P2d 1005 (1941). In *Dunmire*, plaintiff sought to recover damages, including diminished value, for damage to a Packard Hupmobile. The governing policy contained a provision that the insurer would pay "what it would then cost to repair or replace the automobile, or parts thereof, with other of like kind and quality."

In analyzing the language to determine whether a claim for diminished value would stand, the Court determined the word "replacement" meant to restore the property to its pre-accident condition. "Such restoration may or may not be accomplished by repair or replacement of broken or damaged parts. It cannot be said that there has been a complete restoration of the property unless it can be said that there has been no diminution of value after repair of the car." *Dunmire* then looked for guidance to Texas and Minnesota, which also upheld diminished value claims, and determined that a claim for diminished value in this Oregon case would stand.

The most effective way to handle a diminished value claim is to retain an expert quickly to determine how much the value of the vehicle has diminished, if at all.

The *Dunmire* case, despite its age, implies that Oregon may interpret the word "repair" as having a value basis rather than a condition basis. There is room to argue that the insurance companies certainly would have included talk of value in sections calling for repair had they intended to restore the vehicle to its pre-accident value, as opposed to pre-accident condition. However, *Dunmire* may provide a modern day appellate court some justification to decide along the lines of *Mabry*.

Caring for the Chihuahua

In the interim, until Oregon sees a more current appeal of the issue, the courts and arbiters are likely to recognize a claim for diminished value in a first-party setting. Typically, the amounts involved in a diminished value claim are fairly small, subjecting the cases to arbitration claims for attorney fees pursuant to ORS 20.080, as well as the ability for plaintiff to collect attorney fees under ORS 742.061.

The most effective way to handle a diminished value claim is to retain an expert quickly to determine how much the value of the vehicle has diminished, if at all. Based upon the expert's opinion, you can attempt to avoid paying attorney fees by filing an offer of compromise (if your client wants to offer anything). Under ORS 742.061, attorney fees may be avoided if the insurer makes a settlement offer within six months of the claim, and plaintiff does not obtain a better result. Plaintiffs' attorneys frequently are willing to accept an offer of compromise rather than run the risk of a judgment for less than the offer.

In determining the amount of diminution in value, one of the main considerations aside from mileage, is the popularity and availability of the car on the market. The quality of the repairs will be considered, as will whether the repairs were structural or mechanical. In the event of frame damage, even a high quality repair may not fully restore the value because a consumer would be unwilling to purchase a vehicle that sustained such damage. Similarly, if a vehicle was repaired with filler, a consumer may shy away from the vehicle because of the stigma associated with the word "Bondo."

There are two issues for defense counsel to address in diminished value cases. The first issue is the market price of the vehicle. Typically an expert experienced in used car sales, particularly with sales of vehicles that have experienced some damage, are preferable, since they will have some knowledge of

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the impact vehicle damage has on sales price. They also will be able to address the role Kelly Blue Book plays in establishing the fair market value of the vehicle. Many plaintiffs rely on the Kelly Blue Book as evidence of the pre-accident vehicle value, when the Kelly Blue Book does not take into account market forces particular to the region in which the vehicle was located.

An auto body repairman also will prove invaluable to address the nature of the vehicle damage and the quality of repairs. This expert will address whether repairs were performed in accordance with industry standards, whether the vehicle is safe, and whether the repairs were structural or mechanical. Key to faring well on a frame damage or Bondo case is to educate the finder of fact, through the expert, as to the acceptability of the repairs and the unreasonableness of the stigma attached to the words. The auto body expert also can discuss the pre-accident mechanical and structural condition of the vehicle in order to help establish the pre-accident value of that vehicle.

In cross-examining plaintiff's expert, you may wish to focus on the expert's lack of empirical data to support the opinion of the diminished value. In theory, the expert should be comparing the sales price of pairs of vehicles that are otherwise similar except that one has a damage history and the other does not. Experts on diminished value likely have not tracked such differences. You may wish to point out that to properly appraise the value of the vehicle, the standard in the industry would be to compare the vehicle to vehicles for sale that are of like kind and condition. Then question the expert about how many sale vehicles the expert priced that were in the same condition as the post-accident vehicle involved in the case. You may be successful in attacking the qualifications of the expert to testify on diminished value where the expert has no experience in actually selling or tracking comparative sales of damaged and undamaged vehicles. You can also move to strike the expert's testimony as unreliable under OEC 702, 703, and 403 where the expert has failed to utilize recognized appraisal techniques and has provided no data supporting his or her opinion as to value.

The *Mabry* and *Pritchett* cases focus on the key issue: Does the insurer's agreement to repair the vehicle require the insurer to pay diminished value? The *Dunmire* case indicates the answer may be yes.

Conclusion

Diminished value is becoming a popular issue across the nation and is likely to become more hotly contested in Oregon. The *Mabry* and *Pritchett* cases focus on the key issue: Does the insurer's agreement to repair the vehicle require the insurer to pay diminished value? The *Dunmire* case indicates the answer may be yes. However, until an insurer is forced to take the issue to the appellate level, they may be content to let the sleeping dog lie. After all, in at least one state those little dogs have very sharp teeth. ■