

Client Alert

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Florida Supreme Court Finds General Contractor Overhead and Profit are Covered “Replacement Costs” Under Contracts for Homeowners Insurance and Florida Claims Statutes

On July 3, 2013, the Florida Supreme Court held in *Trinidad v. Florida Peninsula Ins. Co.*, No. SC11-1643, 2013 WL 3333823 (Fla. July 3, 2013), that a homeowner’s insurer was required under the language of the insurance policy and Florida claims statutes to include a general contractor’s overhead and profit as part of replacement cost coverage if the insured was reasonably likely to need a general contractor for repairs, even where the insured had not yet replaced or repaired the dwelling.

Background

The case stemmed from a claim for fire damage under a homeowner’s insurance policy. The policy afforded replacement cost coverage under section 1(b) of the policy for replacement of damaged property. The policy also afforded coverage under section 1(c) of the policy for the necessary amount actually spent to repair or replace the damaged building, whichever amount is lower. The insurer admitted coverage for the repair of damaged property and paid the insured the amount it would cost to pay for repairs to the building, but the insurer withheld that portion of the payment representing a general contractor’s profit and overhead. The insurer based the withholding on the belief that these amounts are not due until the insured actually contracts to make the repairs.

The insurer argued, and the lower court agreed, that overhead and profit are not part of replacement costs under section 1(b) of the policy, but were only owed under section 1(c) when actually spent by the insured. Further, the lower court rejected the insured’s argument that the insurer was prohibited from withholding overhead and profit costs by Florida Statute 627.7011(3), which requires an insurer to pay “replacement costs without reservation or holdback of any depreciation in value, whether or not the insured replaces or repairs the dwelling.” The lower court construed the statute as only requiring replacement costs be paid without holdback for depreciation and did not require payment of overhead and profit that had not been incurred.

Holding

Upon review, the Florida Supreme Court reversed the Third District Court of Appeal and held that, under the language of the policy and Florida Statute 627.7011(3), replacement cost insurance includes overhead and profit where the insured is reasonably likely to need a general contractor for the repairs that encompass the covered loss. The court reasoned that the insured would be required to pay costs for a general contractor’s overhead and profit for the completion of repairs in the same way the insured would have to pay other replacement costs in repairing the property.

The court first compared coverage under a replacement cost insurance policy with that under an actual cash value policy. Replacement cost coverage is measured by what it would cost to replace the damaged structure on the same premises. In contrast, actual cash value is generally defined as fair market value, or replacement cost minus normal depreciation. Thus, replacement cost policies provide greater coverage

than actual cash value policies because depreciation is not excluded from replacement cost. The court cited the Florida Second District Court of Appeal decision in *Goff v. State Farm Florida Ins. Co.*, 999 So.2d 684 (Fla. Dist. Ct. App. 2008), where that court had concluded that overhead and profit are like all other costs of repair, such as labor and materials, that the insured is reasonably likely to incur, and they are thus included in the scope of an actual cash value policy where the insured is reasonably likely to need a general contractor. The Florida Supreme Court then reasoned that because overhead and profit are within the scope of actual cash value, those costs necessarily must also be within the scope of replacement cost because replacement cost is broader than and encompasses actual cash value.

The court then turned to whether Florida Statute 627.7011(3), which requires the payment of “replacement costs without reservation or holdback of any depreciation in value, whether or not the insured replaces or repairs the dwelling,” permitted the insurer to withhold payment of overhead and profit costs until the insured actually incurred them. Because the court concluded that overhead and profit are replacement costs where the insured is reasonably likely to need a general contractor for the repairs, it was clear that section 627.7011(3) did not permit an insurer to withhold overhead and profit pending actual repair. However, because section 627.7011(6) permits an insurer to limit its liability to the “reasonable and necessary cost” to repair the damaged property, overhead and profit costs could be withheld absent a showing by the insured that it was likely to need a general contractor for the repairs.

Finally, the court rejected the insurer’s argument that it did not owe overhead and profit expenses pursuant to section 1(c) of the policy, which only covers amounts “actually spent” by the insured. The court reasoned that the insurer had already made a payment under section 1(b) of the policy and had itself acknowledged that its payment was made pursuant to 1(b), which governs the payment of replacement costs when no repairs have been made. Section 1(c) was simply an alternative method of calculating the payment amount when the insured has actually undertaken repairs.

The court remanded the case to determine, consistent with its opinion, whether the insured was reasonably likely to need a general contractor for the repairs encompassing his loss.

Implications

Trinidad supports a broad construction of “replacement costs” to include amounts included in a general contractor’s estimate for overhead and profit, even where those amounts have not yet been incurred by the insured, so long as it is reasonably likely that such costs will be necessary. The opinion also reaffirms the breadth of replacement cost policies as compared to narrower actual cash value policies and provides support for the present recovery of other categories of anticipated, but yet-to-be-incurred costs that might arise in the context of a replacement cost valuation.

Contacts

Walter J. Andrews
wandrews@hunton.com

Lon A. Berk
lberk@hunton.com

Lawrence J. Bracken II
lbracken@hunton.com

John C. Eichman
jeichman@hunton.com

Robert J. Morrow
rmorrow@hunton.com

Curtis D. Porterfiled
cporterfiled@hunton.com

Syed S. Ahmad
sahmad@hunton.com

Michael S. Levine
mlevine@hunton.com

Sergio F. Oehninger
soehninger@hunton.com

William T. Um
wum@hunton.com

Matthew T. McLellan
mclellanm@hunton.com

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