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TECHNICAL ADVISORY

TA # 200

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**SUBJECT:** Louisiana Courts Reject Diminution of Value in Auto Insurance

**BACKGROUND:** Murphy's Law of New Cars works something like this. You hold off trading cars until the last kid is out of college. During those years, your old car never gets so much as a scrape or dent. When you finally get that new car, it's involved in a wreck during the first month. The car's value at the time of the accident was \$35,000, and the repair costs were \$14,500. After the repairs are done, is the car now worth \$35,000 again? Since it's been "wrecked," does it have the same trade-in value?

If the trade-in value was now \$30,000, does insurance cover the "diminution" (reduction) in value of \$5,000?

**MAIN POINTS:** The question of diminution in value relating to auto insurance is not a new one. One of the earliest known cases was in Oregon in 1941, in which it was held that diminution of value was covered as an element of "indemnification." There has been a legal tug-of-war ever since, with insurers and insureds firmly entrenched in their own positions. (One is reminded of the famous quote from Voltaire: "*A long dispute means that both parties are wrong.*")

Authorities indicate that there are three primary sources supporting the argument for diminution of value.

First, if repairs are poorly done, such as paint not matching, some damage appraisal services state that the value of a car can be reduced by as much as 50%. In fact, experts in the appraisal business say that even if repairs are done properly, the car's value can still be reduced by an average of 20%.

Second, some hold the position that the use of non-OEM parts (non Original Equipment Manufacturer), or “after market parts” as they are sometimes called, can reduce the value of the car.

Third is the psychological or perceived reduction in value by the owner, or potential buyer. In the above example, many who have a new car substantially damaged in the first month want to get rid of it and get another new car.

The Internet is starting to play an increasing role in the importance of this third category, with the growing use of on-line services such as CARFAX.com, which allows potential buyers to research the history of a particular vehicle by VIN. Categories checked include accident damage disclosures, flood damage disclosures, salvage, junk, or reconstruction titles, manufacturers recall, and other items.

The question of whether or not insurance should cover any of these reductions in value, real or perceived, has resulted in much litigation.

Interestingly, courts often view claims for diminution of value differently between first party claims and third party claims. Third party claims seem to be much more often recognized in court, in cases where plaintiffs can clearly establish reduced value of their car as a result of the tortfeasor's actions.

Insurers generally oppose diminution of value claims, especially in first party claims, holding that the insurance contract provides only for actual cash value, or repair of like kind and quality. One additional point made by some insurers is that even if diminution of value exists, it is an *indirect* loss, and the insurance contract only covers *direct* loss.

As to first party claims for diminution in value, several courts in Louisiana have recently held that such losses **are not covered** by auto insurance. Two weeks ago, in mid-January of this year, the Louisiana Supreme Court refused to hear appeals on the issue, effectively ending the litigation on the matter.

This decision in Louisiana is in line with similar courts in a number of other states in recent years.

By contrast, the Georgia Supreme Court ruled in November of last year that such claims *were* covered under auto insurance. One industry trade group described the decision as an "aberration."

In response to the increasing litigation over diminution of value, ISO has developed an endorsement, PP 13 01 – Coverage for Damage to Your Auto Exclusion Endorsement, which states that diminution of value claims (“for actual or perceived loss in market or resale value”) are not covered by the PAP.

The endorsement has been approved in at least 38 states. However, several state insurance departments have *rejected* the ISO endorsement, including *Louisiana*, Florida, and Georgia, and others.

The new endorsement might quell future litigation, but legal experts point out that the language has not been fully tested in court yet, so more is sure to come on this issue.

**NECESSARY  
ACTION:**

Please circulate this Technical Advisory to personnel who handle automobile insurance coverage.