

**FLORIDA'S VALUED POLICY LAW:  
DOES A HOMEOWNERS' POLICY COVER EXCLUDED PERILS?**

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One of the enjoyable aspects of an insurance regulatory practice is the complexity of the issues that arise from day to day. Questions that seem straightforward often turn out to be more difficult than they initially appear. Certainly, though, the question presented in the title to this article is the most basic of regulatory questions, right? Once again, a straightforward question meets the complexities of statutory construction, judicial interpretation, and legislative action leaving Florida homeowners' insurers unsure about the extent of their liability when covered and noncovered perils combine to cause total losses to insured properties.

*Interpreting Florida's Valued Policy Law*

The Florida Insurance Code sets forth the Valued Policy Law at Section 627.702, Florida Statutes. The statute provides at subsection (1):

(1) In the event of the total loss of any building . . . located in this state and insured by an insurer as to a covered peril . . . the insurer's liability, if any, under the policy for such total loss shall be in the amount of money for which such property was so insured as specified in the policy and for which a premium has been charged and paid.<sup>1</sup>

Florida's Fourth District Court of Appeal altered insurers' historical notions of this statute in the 2004 case *Mierzwa v. Florida Windstorm Underwriting Association*.<sup>2</sup> The case involved an insured whose home sustained wind and flood damage during Hurricane Irene in 1999. The homeowner had wind insurance in the face amount of \$281,000 from the Florida Windstorm Underwriting Association ("FWUA"). The homeowner separately purchased a flood insurance policy from another insurer. The homeowner made claims under both policies. The FWUA determined the amount of wind damage to be \$64,807 plus \$8,370 for ancillary coverages. The flood insurer determined the flood damage to be \$54,485. Thus, the insurers evaluated the combined wind and flood damage as \$127,662, with wind repairs comprising 57% of the total.<sup>3</sup>

A local ordinance specified that if the total damage to a dwelling exceeded half of its value, the dwellings were required to be rebuilt rather than repaired. Although the face amount of the wind policy was \$281,000, local officials determined that the cost to repair the dwelling would exceed half of its value. It is unclear how the local officials determined the dwelling's pre-loss value for these purposes. Nonetheless, based upon this constructive total loss, the insured sought coverage from the FWUA for the face amount of the wind policy (\$281,000) under the Florida's Valued Policy Law. The FWUA responded that it was responsible for only its pro rata portion of the damage. The trial court agreed, but the Fourth District Court of Appeal ruled that the FWUA indeed was responsible for the full face amount of the policy plus additional law and ordinance coverage. The court observed that under the Valued Policy Law, "[i]f the FWUA has any liability at all, even a fractional share of the total damage, under the [Valued Policy Law] it is liable for the face amount."<sup>4</sup>

The appellate court rejected the FWUA's position that a policy exclusion for flood damage justified a pro rata payment. Because flood and wind combined to cause the total damage, the FWUA reasoned that it should be responsible for only the portion of the claim allocable to wind damage. The court responded that the flood exclusion in the policy at best created an ambiguity between the policy and the Valued Policy Law. The court resolved this potential ambiguity in favor of the insured.<sup>5</sup> Thus, the *Mierzwa* court determined that if an insurer is responsible for any portion of a total loss to a dwelling, the insurer must pay the policy limits without regard to other causes of loss. As seen in *Mierzwa*, this can be particularly troubling when local ordinances cause damaged dwellings to be declared constructive total losses because estimated costs of repair exceed 50% of the dwellings' values.

In addition to concerns that *Mierzwa* essentially results in insurers becoming responsible for noncovered perils, the decision also summarily declared the FWUA responsible for the entire ordinance and law limit without any finding that the insured suffered increased repair costs. The FWUA policy provided that the insured could recover an additional 25% of policy limits in excess of the face amount for increased costs of rebuilding attributable to changes in local building codes after the dwelling's original construction. The *Mierzwa* court found "if the building is deemed a total loss for the purpose of the [Valued Policy Law] it should certainly be deemed a total loss for purposes of this ordinance or law coverage."<sup>6</sup> The court therefore awarded the additional 25% in benefits without any indication in the opinion that the insured actually incurred increased costs of reconstruction due to changed building codes.

### ***Remaining Questions After Mierzwa***

Although the *Mierzwa* decision presents the possibility of unforeseen liability for insurers, the decision also leaves key issues unresolved that ultimately might limit this new exposure. First, the court observed that 57% of the repair costs were attributable to wind damage and the remainder to flood. The court stated that if the FWUA had "any liability at all, even a fractional share of the total damage," it was responsible for policy limits. In a footnote, however, the court pointed out that because the FWUA covered more than half of the damage, it had no occasion to consider the "parade of horrors" that could arise, for example, if a covered peril were to account for only 1% of the total damage.<sup>7</sup> This has led some wind insurers to interpret *Mierzwa* as applying only to total losses in which wind damage is the predominant cause of loss.

The *Mierzwa* court also acknowledged the desire of insurers to limit their exposure to only perils they contract to insure. The court suggested that limiting the effect of the Valued Policy Law is "arguably possible" through expressly worded policy provisions.<sup>8</sup> However, the court noted even such a policy change might not be sufficient to overcome application of the Valued Policy Law. Further, the court recognized that insurers would be required to obtain regulatory approval for contract changes of this type.

### ***Wind and Flood Claims During the 2004 Hurricane Season***

The *Mierzwa* decision was issued June 23, 2004, and rehearing was denied on August 12, 2004. The next day, the first of Florida's 2004 hurricanes made landfall. These hurricanes, and Hurricane Ivan in particular, produced large numbers of claims in which flood and wind combined to cause actual or constructive total losses to insured homes. Building code requirements in these coastal communities have increased since many of the damaged dwellings were built, causing reconstruction estimates that exceed the face amount of the insureds' wind policies. In some cases, policyholders might not have carried flood insurance leaving the homeowners' policy as the only potential source of recovery. These factors, along with a general awareness of the recent *Mierzwa* decision, have prompted many insureds to seek policy limits from their wind insurers even when flood contributed to or was the larger cause of the insureds' losses.

Many insurers have disagreed with or distinguished *Mierzwa* as they have adjusted claims arising from the 2004 hurricane season. As an appellate case from Florida's fourth district, *Mierzwa* is persuasive but not controlling areas of the state where most of the claims involving both wind and flood damage occurred. In addition, more of the damage is attributable to flood than wind in a large number of the 2004 flood claims. These factors have prompted lawsuits seeking policy limits under the Valued Policy Law for the total losses attributable to the combination of flood and wind. The most widely publicized of these cases is *Scylla Properties, LLC v. Citizens Property Insurance Corporation*.<sup>9</sup> The *Scylla Properties* plaintiffs filed a class action against Citizens Property Insurance Corporation ("Citizens") seeking policy limits under the Valued Policy Law for residential buildings that were actual or constructive total losses as a result of the 2004 hurricanes. The proposed class plaintiffs alleged the following common questions of law or fact in their Amended Complaint:

- (i) If a building or other structure is insured as to a covered peril, does the Valued Policy Law mandate that the carrier is liable to the owner for the face amount of the policy, no matter what other facts are involved as to the cost or repairs or

replacement, where the carrier has “any” liability and the property is rendered a “total loss.”

- (ii) Whereas the Valued Policy Law requires [Citizens] to pay the face amount of the policy for a total loss if [Citizens] has “any” liability for that loss, does the Valued Policy Law require that a covered peril substantially caused the entire loss, or does it require merely that a covered peril contributed to the loss.<sup>10</sup>

The parties filed an Agreed Motion for Class Certification. Notwithstanding their general agreement on class certification, Citizens urged that policyholders in the fourth appellate district where *Mierzwa* was decided should be excluded from the class. The plaintiffs sought to exclude those policyholders from the class to avoid jeopardizing the impact of *Mierzwa* as controlling precedent in those counties. Citizens also asserted, and the plaintiffs disagreed, that the class should be divided into subclasses consisting of (a) insureds whose losses attributable to wind damage were less than their deductibles, (b) insureds whose losses attributable to wind damage were in excess of their deductibles but less than 50% of the value of their properties, and (c) insureds whose losses attributable to wind damage exceeded 50%, but were less than 100%, of the value of their properties.<sup>11</sup>

The trial court in *Scylla Properties* agreed with the plaintiffs that policyholders in counties comprising the fourth appellate district should be excluded from the class, but agreed with Citizens that the class should be divided into the three subclasses.<sup>12</sup> The court found that common questions of law and fact among the members of the class predominate over any individual questions the class members could raise. The court specifically identified the following common questions of law or fact:

- (i) Whether the Valued Policy Law requires payment of the policy limits under the policy in the event of a total loss so long as there was any amount of windstorm damage to the insured property for which Citizens is liable; and
- (ii) Whether Citizens is entitled to a setoff from its policy limits for the amount of flood insurance benefits received by an insured in any of the above circumstances.<sup>13</sup>

The plaintiffs have filed for limited reconsideration asserting there are no members of subclass (a)(persons with wind damage less than the amount of their deductibles). The next hearing in the case is scheduled for late May. Even proceeding on an expedited schedule, the *Scylla Properties* case is unlikely to bring clarity to insurers’ obligations under the Valued Policy Law for many months.

#### ***The Legislative Response:***

The Florida’s Legislature convened for its 2005 regular session in early March and will meet until early May. Legislative proposals surfaced that would have “clarified” the legislative intent behind the Valued Policy Law as limiting insurers’ liability to the amount of losses attributable to covered perils. These clarifications were designed to apply retroactively and avoid the *Mierzwa* result on 2004 claims. Although statutory amendments generally apply only prospectively, changes can apply retroactively if the legislature evidences a clear intent to do so and retroactive application is constitutional.<sup>14</sup> In particular, if an amendment is enacted soon after a controversy involving the interpretation of a statute, a court may consider the amendment as a legislative interpretation of the original law and not as a substantive change.<sup>15</sup>

Consumer representatives and trial lawyers opposed retroactive clarifying amendments to the Valued Policy Law. With considerable debate throughout the process, the legislature has added, removed and changed draft amendments to the Valued Policy Law several times. As of this writing, two weeks remain in the legislative session and the issue is not resolved.<sup>16</sup> The Senate and House of Representatives currently are moving forward with different proposed amendments to the Valued Policy Law. The Senate would add the following:

(1)(b) The legislative intent of this subsection is not to require an insurer to pay for a loss caused by a peril other than a covered peril. In furtherance of such legislative intent, when a loss was caused in part by a covered peril and in part by a noncovered peril, the insurer's liability under this section is limited to the percentage of the loss caused by the covered peril.<sup>17</sup>

The House of Representatives would add the following statement to the Valued Policy Law:

(1)(b) The intent of this section is not to deprive an insurer of any proper defense under the policy, to create new or additional coverage under the policy, or to require an insurer to pay for a loss caused by a peril other than the covered peril. In furtherance of such legislative intent, when a loss was caused in part by a covered peril and in part by a noncovered peril, paragraph (a) does not apply. In such circumstances, the insurer's liability under this section shall be limited to the amount of the loss caused by the covered peril.<sup>18</sup>

Differences in the Senate and House of Representatives' amendments will be resolved in a conference committee if the chambers pass inconsistent bills. As with all versions of the proposed amendments debated throughout the 2005 legislative session, the final version of any amendment is likely to trigger debate as to its potential retroactive effect and its anticipated impact on rates and capacity.

### ***Conclusion***

The Fourth District Court of Appeal's decision in *Mierzwa v. Florida Windstorm Underwriting Association* surprised the insurance industry when it revealed the century-old Valued Policy Law could result in liability for losses beyond those attributable to covered perils. The industry unfortunately had little time to react to *Mierzwa* before four hurricanes made landfall in Florida. *Mierzwa* is not controlling authority in Florida's Panhandle where most of the 2004 claims involving wind and flood damage arose. The absence of controlling authority, combined with factual distinctions in the claims and differing legal views of the Valued Policy Law, have prompted litigation that will take months and perhaps years to resolve. The Florida legislature could have diminished the impact of this litigation by adopting an amendment clarifying that the Valued Policy Law does not require insurers to pay losses beyond those attributable to covered perils. However, it is unclear as the 2005 legislative session wanes whether any amendment adopted by the legislature will apply retroactively or only prospectively. Assuming this uncertainty remains, litigation over the proper application of the Valued Policy Law will continue for many more months through Florida's trial and appellate courts.

### ***Endnotes***

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<sup>1</sup> S. 727.702(1), Fla. Stat. (emphasis added).

<sup>2</sup> *Mierzwa v. Florida Windstorm Underwriting Association*, 877 So. 2d 774 (Fla. 4<sup>th</sup> DCA 2004).

<sup>3</sup> *Id.* at 776.

<sup>4</sup> *Id.* at 778.

<sup>5</sup> *Id.*

<sup>6</sup> *Id.*

<sup>7</sup> *Id.* at 778 n.5.

<sup>8</sup> *Id.* at 778.

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<sup>9</sup> *Scylla Properties, LLC, and William D. Clark, Jr., on their behalves and on behalf of others similarly situated v. Citizens Property Insurance Corporation*, Case No. 05 CA 01. Citizens Property Insurance Corporation is Florida's residual property insurance market and writes policies of the types formerly written by the FWUA and the Florida Residential Property and Casualty Joint Underwriting Association.

<sup>10</sup> *Scylla Properties, LLC v. Citizens Property Insurance Corporation*, Amended Complaint pp. 8-9.

<sup>11</sup> *Scylla Properties, LLC v. Citizens Property Insurance Corporation*, Stipulation of Contested Matters as to Certification of Class, pp. 2-3.

<sup>12</sup> *Scylla Properties, LLC v. Citizens Property Insurance Corporation*, Findings and Order Certifying Class.

<sup>13</sup> *Id.*

<sup>14</sup> *Memorial Hospital-West Volusia, Inc. v. New-Journal Corp.*, 784 So. 2d 438, 440-41 (Fla. 2001).

<sup>15</sup> *Lowry v. Parol & Probation Comm'n*, 473 So. 2d 1248, 1250 (Fla. 1985); *see also Kaplan v. Peterson*, 674 So. 2d 201, 205 (Fla. 5<sup>th</sup> DCA 1996).

<sup>16</sup> Updates regarding changes to Florida's Valued Policy Law will be posted periodically at [www.radeylaw.com](http://www.radeylaw.com).

<sup>17</sup> CS/CS/SB 1488.

<sup>18</sup> CS/HB 1937.