THE INADEQUACIES OF THE DIMINUTION OF VALUE APPROACH TO DAMAGES TO REAL PROPERTY IN TORT CLAIMS

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Generally speaking, the purpose of tort damages is to make an injured party whole and restore the injured party, as nearly as reasonably possible, to the position in which he or she would have held absent the injury.[1] When dealing with damages sustained to real property, most jurisdictions provide that the cost to repair the property is the proper measure of damage so long as the cost to repair does not exceed the diminution in value, which is the difference between the fair market value immediately before and immediately after the damages are sustained.[2] However, application of this general rule can sometimes result in inadequate compensation for the injured party. While the rationale behind the general rule is an attempt to prevent an injured party from being overcompensated for the damages actually sustained, applying the rule in a rigid and formulaic manner can result in a wrongdoer paying far less than is just given his/her tortious act. Some jurisdictions recognize that the rigid application of this general rule is inadequate, but many others continue to apply it without consideration of whether the remedy adequately compensates the injured parties.

As more jurisdictions are recognizing that the diminution in value approach to damages does not always afford a proper measure of damages caused by the tortfeasor, the subrogation professional must be cognizant of the how the Courts may ultimately handle this issue, and obtain the information necessary to establish the appropriate level of damages during the adjustment of the claim.

The most common application of an alternative measure of damages was initially applied in cases where the property had a "special purpose," and therefore, there was no active market to determine the diminution in value. However, Courts are expanding the exception to the general rule more often. Unfortunately, in order to get a Court to allow for damages in excess of the diminution of value, an injured party must first establish a basis to avoid the application of the general rule. The most common way to avoid the application of the general rule is to establish that there is not an active market for the damaged property, and therefore, the diminution of value is not capable of being calculated. However, Courts have also allowed injured parties to establish that there is a "personal reason" to restore the property to its pre-injury condition. This "personal reason" contention initially arose in consideration of damage to land, but courts have been willing to expand this "personal reason" rationale to damage to improvements to real property. In allowing for a damage award in excess of the diminution of value, Courts general hold that the general rule should

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[1] Restatement of Torts 2d, s 901 (1979).

[2] *See e.g.* Blanton & Co. v. Transamerica Title Ins. Co., 536 P.2d 1077, 1080 (1975); Charles v. Rueck, 3 Cal. Rptr. 490, 491-92 (1960); Kirst v. Clarkson Constr. Co., 395 S.W.2d 487, 493-94 (Mo.Ct.App.1965); Newsome v. Billups, 671 S.W.2d 252, 253-55 (Ky.Ct.App.1984); Stony Ridge Hill Condominium Owners Ass'n v. Auerbach, 410 N.E.2d 782, 784, 788 (1979); Mozzetti v. City of Brisbane, 136 Cal. Rptr. 751, 757 (1977).

be considered a guide to determining the proper measure of damages, but should not be an absolute limit on damages.

> [R]ules governing the proper measure of damages in a particular case are guides only and should not be applied in an arbitrary, formulaic, or inflexible manner, particularly where to do so would not do substantial justice.[3]

Those jurisdictions that do not apply the diminution in value limitation to all cases are not necessarily holding that the diminution of value is not the proper measure of damage, but merely recognizing that in certain situations, the diminution in value does not return an injured party to his/her pre-injury condition, which is the stated goal of tort law.

> To hold that [an injured party] is without remedy merely because the value of the land has not been diminished, would be to decide that by the wrongful act of another, an owner of land may be compelled to accept a change in the physical condition of his property, or else perform the work of restoration at his own expense.[4]

While a majority of the cases allowing for damages in excess of the diminution in value involve damages to land, as opposed to improvements to real property, the rational utilized in these cases can be applied to damages sustained to improvements to real property.

> Limiting the costs of repairs to the diminution in value of the property appears to fly in the face of [the rule requiring that the injured party be restored to his former position]. The diminution in value may be slight because the injury is slight as compared to the total property, as evidenced by this case…Yet, should we therefore excuse the tortfeasor from any liability? Is the owner not entitled to have his building [undamaged] even though the total value remains unchanged? We think so.[5]

Unfortunately, there are still may Courts that continue to apply the diminution in value as the proper measure of damage in an arbitrary and formulaic approach, which, in certain situations, does not adequately compensate an injured party, nor does it put an injured party in its pre-loss condition.

In those situations where the cost of repair exceeds the diminution in value, it is possible that a Court will apply the general rule to limit an injured party's recovery. However, the subrogation professional should not automatically concede to the limitation. In certain circumstances, Courts may allow for damage awards in excess of the diminution in value. In order to obtain a damage award for the costs of repairs in excess of the

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[3] Myers v. Arnold, 233, 403 N.E.2d 316, 321 (Ill. 1980)
[4] Heninger v. Dunn, 162 Cal. Rptr. 104, 108 (1980), *quoting* Dandoy v. Oswald Bros. Paving Co., 298 P. 1030, 1031 (Cal. App. 1931).
[5] L Invs., Ltd. v. Lynch, 322 N.W.2d 651, 656 (Neb. 1982).

diminution in value, the injured party must demonstrate that the repairs are "practical" and "reasonable,"[6]

If an injured party intends to seek the cost of repair in his/her cause of action, it is still necessary to demonstrate the diminution in value. Failure to establish the diminution in value could negatively impact an injured party's recovery efforts. Even in those jurisdictions that allow for damage awards in excess of the diminution in value, presenting evidence of the diminution in value is still a necessary aspect of proving your damages. If an injured party fails to establish the diminution in value, and the Court does not find that the injured party has established that an exception to the general rule, an injured party could be in a position where it has failed to present any evidence regarding its damages. Furthermore, Courts may refuse to award the cost to repair if the expenses to repair or restore the property are considered to be exorbitant compared to the diminution in value resulting from the damages.[7]

The holdings in those cases allowing for damages in excess of the diminution in value recognize the need for a flexible approach to damages to further the stated goals of tort damages. "Bearing in mind that the principle underlying allowance of damages is to place the injured party in the same position, so far as money can do it, as he would have been had there been no injury or breach of duty, that is, to compensate him for the injury actually sustained."[8]

While the diminution of value approach to damages to real property is still the general rule in most, if not all, jurisdictions, in certain circumstances, the limitation on damages can be avoided if the subrogation professional is able to demonstrate a rational and reasonable basis to allow for the cost of repair even in excess of the diminution in value. If it is clear that the diminution of value will not adequately compensate the injured party, the Court may allow for damages in excess of the diminution of value, but this exception to the general rule is not without limits. If the cost of repair is well in excess of the diminution of value, it is possible that the Court could hold that the cost of repair is disproportional to the damages sustained, and apply the diminution of value approach to damages, even if it does not adequately compensate the injured party.

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[6] Heninger*. supra at 861; see also,* Rector of St. Christopher's Episcopal Church v. McCrossan*,* 235 N.W.2d at 611; and *Myers, supra*

[7] *Heninger, supra* ($241,257.00 to restore trees and undergrowth "manifestly unreasonable" in relation to land value which increased from $179,000.00 to $184,000.00); Maloof*, supra* (cost to replace vegetation limited to $77,660.00 to approximate but not duplicate actual pre-existing condition);

[8] Golden Sun Feeds, Inc. v. Clark, 682, 140 N.W.2d 158, 161 (Iowa, 1966).