

PROTECT YOUR PUBLIC ENTITY POOL WITH ACCURATE PROPERTY VALUATIONS



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Accurately determining a property's value can be a challenge—however, if not done correctly, it can have serious consequences. Inadequate or inaccurate property valuations can lead to financial surprises in the aftermath of a loss, which can also affect your pool's bottom line.

Property valuation is the process of determining the replacement cost value of a property and its contents for coverage purposes. Although there are different methods for determining a building's value, replacement cost is the most common and widely accepted valuation approach. Building replacement cost covers the cost to repair or replace a building with materials of like kind or quality and does not include the value of the land. It is important to note that it is not purchase price or tax/book value. Contents valuations can be more complex, as equipment replacement time varies widely and needs to be researched in more detail. If calculated correctly, these total insurable values (TIV) should capture the size and scope of a pool's property exposures. Property valuations are generally provided to the pool in a statement of values (SOV).

A Challenging Property Market Further Highlights Underreporting of Property Values

Determining accurate and defensible property values is essential for property coverage and serves as one of the primary factors that drives reinsurance underwriting decisions. It is important to remember that reinsurers use reported pool values to determine capacity, terms, pricing, structures and models, and catastrophe rates. Therefore, if pool values are underreported, the risks will outweigh the contributions collected and could affect a pool's ability to pay claims.

Providing accurate property values is not only important to your overall risk assessment, but there is also a reputational risk at stake. Inaccurate reporting can result in a reinsurer losing trust in your pool. This could result in stricter terms that are more unfavorable to your members.

When a carrier questions the building values reported, they may run their own building valuations and require an amendment of values or charge contributions based on the often higher values. This can substantially increase an expected renewal for your pool.

The Importance of Standardized Reporting

In addition to underreported values, another issue we see regarding property valuation is nonstandardized reporting methodology. Gathering figures for the SOV is seldom done by one person. There are often multiple individuals within an organization that contribute to building out the SOV, including members and pool staff. Therefore, a standard should be enforced when gathering the data. For instance, it is important to make sure that everyone uses the same calculation to determine the inflation rate. Establishing a consistent quality standard across all channels will ensure that you obtain the most accurate data.





Increase Your Chances of Getting the Best Property Values With Appraisals

Appraisals help ensure that your pool is properly covered by reducing potential liability from undervalued property, and also minimize potentially inflated contribution costs from overinsuring overvalued property. Appraisals can be done by professional companies who specialize in the field and public entities, or by loss control professionals on staff at your pool or pool administrator. If you use a professional, it is important to use a reputable company that adheres to the Uniform Standards of Professional Appraisal Practice (USPAP) and the Code of Professional Ethics and Standards of Professional Practice of the Appraisal Institute.

Benefits of getting an appraisal can include the following:

- » Confirm accuracy of building square footage, construction materials/components, construction quality, etc.
- » Accurately reflect current valuation for new building construction or renovations that have been completed.
- » Provide documentation for proof of loss.
- » Provide confidence to reinsurers that the values were determined by an experienced, unbiased professional. This differentiator could lead to greater market access, better terms and conditions, more program options, and improved underwriting results.
- » Offer due diligence to help support the pool board's decision-making when considering alternative policy structures, deductible options, and multicarrier shared and layered programs.

Updated appraisals are recommended every three to five years to keep values current. Consider dividing the buildings your pool covers into appraisal groups that are rotated evenly so each property is appraised every three to five years. It is important to note that most

appraisal firms will not trend up an appraisal that's more than five years old.

The additional costs associated with LEED-certified buildings are generally not included in standard replacement cost appraisals. If your pool covers LEED-certified buildings, your appraisal needs to be amended to include building enhancements if they are significant enough to have a discernable impact on building cost. This might consist of engineered wood and composite construction materials, green roof systems, special window treatments and glazing, specialized plumbing and fixtures, greywater systems, and many other components. These additional features should be accounted for, and value added to the structure to reflect the correct replacement cost.

Another best practice is to review construction trend factors and inflation annually, and adjust appraisal values accordingly. This approach will generally provide a relatively accurate adjusted value.

Our partner, Gallagher Bassett Services, provides proven valuation methods that appraise buildings, contents, machinery, equipment, furniture, fixtures and leasehold improvements to establish true insurance replacement values. They offer a cost estimator report and value verification form, along with orderly and forced liquidation appraisals. Their process includes:

- » Establishing the proper level of insurance coverage
- » Maintaining up-to-date appraisals
- » Assisting clients in the claims process if a loss occurs

To learn more, visit www.gallagherbassett.com.

Can't Get an Appraisal? Use Validated Tools and Reference Guides

If you cannot get a physical appraisal, a desktop valuation platform can be a useful tool for identifying anomalies in valuation—just remember that it's only as accurate as the data entered. Valuation tools require the user to make certain subjective assessments and incorporate generic assumptions that may not be appropriate for a particular building.

Another way to determine the value of a property is to use the cost of new construction. The replacement costs your pool reports for older properties should align with the costs of constructing a similar building today, in the same geographic region, using current construction materials and adhering to current standards. If you calculate using this method, it is important to consider the direct costs (materials and labor) and the indirect costs (taxes, administrative fees, financing costs, professional fees, etc.). Whatever valuation method you choose, your broker or reinsurance partner can work with you to ensure the most accurate value for your pool's total property exposure.





Conclusion

2020 was impacted by catastrophic events such as hurricanes, wildfires, a pandemic and much more. These events have (and will) continue to impact the property insurance marketplace, and we have seen more focus on valuations as loss trends have continued to outpace pricing models. The best way to protect your pool is to follow the tips described in this paper to provide the most accurate information to your pool broker and underwriter. Otherwise, underwriters will use their own discretion to determine values and corresponding rates in the absence of verifiable data. A measured, collaborative approach with your broker to review and update values will help your pool secure the right coverage at the best possible member contribution.

SOURCES:

https://axaxl.com/fast-fast-forward/articles/property-perspective_why-accurate-property-valuations-matter-and-three-ways-to-get-the-right-numbers?utm_campaign=NA_USA_FFF_SNA_BNA_eBlast_Email_October_2020&utm_medium=email&utm_source=Eloqua

Monitoring Key Trends and Finding an Optimal Approach to Property Valuation by Global Risk Consultants



Martha Bane

About the Author

Martha Bane is the managing director of Gallagher's Property practice and a principal in the Real Estate & Hospitality practice. She started her career in insurance in 1994 with General Star Insurance Company. Martha spent six years as a property and inland marine underwriter with Chubb. She specialized in underwriting large national and international property and builders risk programs for real estate, hospitality, healthcare, higher education, financial and municipal clients.

Martha has used this experience to structure, negotiate, and implement large national property and builders risk programs, with an emphasis on catastrophic exposures. Her expertise with complex layered and quota-share programs, as well as senior insurer relationships, helps deliver innovative insurance and risk management property solutions to Gallagher's clients.

Martha also manages Gallagher's Los Angeles Real Estate & Hospitality team. The team is made up of 35 insurance professionals specializing in property, casualty, environmental and financial products for Gallagher's real estate and hospitality clients. They currently place coverage in the worldwide insurance marketplace for clients with more than \$150 billion in insurable values.

Martha has spoken at numerous industry events on a variety of property insurance-related topics. *Intelligent Insurer* recognized her as an influential woman in reinsurance in 2017, and she received the Women to Watch Award from *Business Insurance* in 2020.

Martha Bane

Managing Director, Property Practice

martha_bane@ajg.com

818.539.1444