

# ERRORS & OMISSIONS

## RISK MANAGEMENT ALERT

### Be Aware of the Growing Concern of Insurance to Value

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Several recent industry articles have noted that many personal and commercial properties are potentially vastly undervalued and underinsured. An article from GenRe, authored by James Kenworthy and Shannon Dowd, reported that **upwards of 60% of homes and 70% of commercial buildings are undervalued – primarily because the cost of building materials has risen significantly over the last 6-12 months.**

The GenRe article and a recent Wall Street Journal article noted the following:

- Lumber costs up 50%-100%
- Labor costs up 8%
- Crude oil, a major component of paint, roof shingles and flooring, up 80% from October 2020
- Prices for granite, insulation, concrete blocks and brick at record levels
- Costs up \$9,000 per unit for apartment construction
- Rising costs for PVC production/availability due to recent hurricanes

#### The Potential for Claims Issues

For many years, **E&O claim statistics have shown that issues involving personal property (HO, Dwelling coverage, etc.) and commercial property have been a leading cause of E&O claims.** Because the values are traditionally higher in commercial property, the losses can be among the most significant, so simply applying an increase property limit factor at renewal may not be enough.

This means that virtually every agency likely has some customers whose property insurance values are insufficient, potentially resulting in claim issues at the time of a loss.

#### Choosing Limits and Your Role in It

Virtually every E&O carrier follows the premise that customers should choose their own property values, with agents/brokers, outside appraisers and various valuation services offering information customers can reference. This provides an element of protection for the agency if a problem arises. **It is highly recommended on commercial accounts, and it is suggested that a property disclaimer be provided annually to commercial accounts. In addition, agencies should require customers to sign an applicable statement of value forms.**

Valuing contents has long been an issue because of the lack of standard industrywide tools available to evaluate most contents exposures. This is another area where customers must play a pivotal role in determining property limits. Issues including the following have been noted:

- Machinery and equipment reconstruction costs that may be significantly more expensive as replacement parts might no longer be available
- Contents customized for the operation
- Discounts and concessions no longer available from suppliers/original equipment manufacturers (OEMs)

Some articles raise serious concerns for agents who use various insurance-to-value tools and benchmarks as these tools may be outdated and not reflect current conditions. **Plus, it is important to distinguish between replacement cost and reconstruction cost.** The key item addressed and factored into some valuation tools states that reconstruction cost includes “additional expenses related to repair and restoration contractors’ fees, the construction process itself, the location of the property, demolition costs and debris removal.” These factors create a higher valuation than a new construction.

Agencies should have dialogue with their customers about this issue, which can help to minimize the problem if a customer suffers a loss that is not adequately covered.

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