Insured Values and Co-Insurance

The basis upon which claims for loss or damage to Insured property are settled is an important aspect of property insurance policies. Policies specify how the lost or damaged property will be valued, such as Replacement Cost or Actual Value. They also have conditions specifying how the property can be replaced as well as penalties that apply if the property was not insured to its full value. It is important that these conditions are understood when the policy is purchased and limits of insurance are determined.

1. Replacement Cost

Replacement Cost means that in the event of loss or damage you are covered for the full replacement cost with new materials of like kind and quality, regardless of the age of the damaged property, and with no deduction for depreciation. The policy should also include any additional cost of construction to comply with municipal by-laws regulating the construction, demolition and debris removal and the value of any undamaged portion of the building that has to be removed.

This means old property is replaced with brand new buildings and equipment regardless of their age and the policy should also cover any additional costs to bring the building up to current code.

2. Actual Cash Value

Actual Cash Value, often referred to as ACV, is the actual value of the property at the time of loss taking into account depreciation. This can often be a fraction of the replacement cost value, particularly on older property. It is the most the insurer will pay regardless of the amount of insurance on the policy.

3. Insuring Your Property

You are responsible for determining the amount of insurance required. Often the help of an appraisal company is needed and appraisers can be engaged to determine values strictly for insurance purposes. You will need to establish the correct values for both your buildings and contents. Contents include furniture, fixtures and fittings, equipment and stock. In addition to these physical assets, you should also have business interruption insurance to protect against a loss of income in the event of insured loss or damage to the property. This type of insurance also pays for the cost of continuing expenses during the period your premises are shut down.

For example if the business is shut down due to a fire, the policy will pay your loss of profits. It will also the pay the bills that continue regardless of the fact that you shut down and are no longer earning any income. These expenses are referred to as standing charges.

4. Statement of Values

The policy is issued in accordance with a Statement of Values. This is a statement that you attest to and sign. It details the property you want to insure and the value you have established for each item. The insurer relies on this information to set their rates along with other information that has been provided about the business and property you are insuring.

5. What is the Correct Amount of Insurance on a Replacement Cost Basis?

The policy requires that you insure for the full replacement value of the insured property, both buildings and contents. It is important to insure the full replacement cost value of the buildings and contents.The amount should include the cost to replace with materials of like kind and quality with the exercise of due diligence and dispatch.

This sounds a bit technical but it means that the amount of insurance you select must reflect current building costs to replace the property as it was prior to the loss. It takes into account that you would want to replace the property as quickly as is reasonably possible.

6. What Happens if we Don’t Insure for the Correct Amount?

The limit on the policy is the most the insurer will pay in the event of a loss or damage.If you suffer a total loss (or constructive total loss) of the property insured and the actual replacement cost exceeds the limit on the policy you will be responsible for the difference.

This simply means the insurer is not going to pay more than the amount of insurance you selected. A Total Loss is when the amount of damage destroys the entire property or, if the amount of damage exceeds the limit on the policy, which is known as a constructive total loss.

Here is a total loss example where the amount of Insurance purchased is less than the actual replacement cost:

Amount of Insurance

• Building Insurance	$1,000,000
• Contents Insurance	$50,000
• Total Insured Amount	$1,050,000

Actual Replacement Cost

• Building Construction	$1,500,000
• Replacement of Contents	$150,000
• Total Loss	$1,650,000

Settlement

• Insurer pays:	$1,050,000
• You pay:	$600,000

This shows how critical it is to select the correct amount of insurance and that skimping on coverage to save premiums can have a devastating effect in the event of a claim.

7. **Does the Policy Have Coinsurance Penalty?**
   Most policies do contain a co-insurance clause which will reduce a loss settlement in the event it is determined the actual value exceeded the amount of insurance you selected. The coinsurance can sometimes be replaced with a Stated Amount Clause, which simply states that the insurer has accepted the declared values as being accurate and there will be no co-insurance penalty as long as you insure to the full value you have declared on the statement of values. It is typically a requirement to have a reasonably current appraisal before insurers will offer a Stated Amount clause.
8. **How Does Coinsurance Work?**
   The purpose of this clause is to encourage insurance to be bought to the correct value. If the property is underinsured and should a claim occur, a penalty can be applied even in the event of a partial loss. Many policies contain a 90% coinsurance clause which means you must be insured to at least 90% of the correct value in order to avoid the penalty. If you are underinsured a penalty will be applied in the event of a partial loss.

This is how it works in a partial loss, such as a fire in the kitchen that doesn't destroy the building completely but causes extensive damage.

For the sake of this example let's assume the loss (replacement cost of the damaged property) is $500,000:

Amount of Insurance

• Building Insurance	$1,000,000
• Contents Insurance	$50,000
• Total Insured Amount	$1,050,000

Actual Replacement Cost

• Building Construction	$1,500,000
• Replacement of Contents	$150,000
• Total ReplacementCost	$1,650,000

The minimum amount of insurance to avoid the coinsurance penalty is $1,650,000 X 90% = $1,485,000.

The insurer will divide the actual amount of insurance on the policy by the minimum amount to come up with the coinsurance penalty.

The simple equation is as follows:
The amount of insurance you have: $1,050,000 divided by:
The minimum amount you needed: $1,485,000 x the loss ($500,000) = $353,535

Insurer Pays: $353,535
You Pay: $146,4655

9. Do we Have to Insure for the Full Replacement Cost?

Some policies offer coverage on an Actual Cash Value basis. This means the insurer will not pay the full replacement cost in the event of claim but will deduct accumulated depreciation. On older buildings this may be substantial and it will mean that you will not be able to afford to replace your building in the event of a total loss and if you suffer a significant partial loss you will likely be responsible for paying a very large portion of the repair bill.

10. Will the Appraisals Result in Increased Premiums?

If your property is correctly valued, then no change should be necessary. If the coverage amounts are currently underinsured your values will be increased and this will result in an additional premium. The amount of the increase in premium will depend on the amount by which the values need to be increased. However, a small increase in premium is nothing compared with the difficulties that arise in the event of an underinsured loss.

Next Step?

Let's engage in dynamic discussion around the factors and variables that are unique to your business so we can obtain the best product, from reliable and stable insurers to meet your needs.

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Mining Team

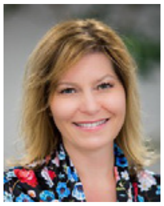
Clive Bird

Clive is an insurance risk specialist, investor, entrepreneur, and product developer for bespoke insurance risks. For over 15 years Axis Insurance enjoyed a reputation for quality, innovation, creativity and relationship building.

Clive began his Insurance career at Lloyd's of London, renowned for its technical underwriting expertise and a creative approach to risk, providing him with opportunities to push the boundaries of product innovation. Moving to the West Coast of Canada, he has expanded his broad Insurance knowledge and London market relationships to produce products for Canadian clients working across the globe.

Clive has worked extensively with public companies with a strong focus on mining and mineral exploration industry, addressing the broad range of risk exposures they face worldwide. Dynamic business enterprises are starved for the innovation and market relationships Clive can deliver. As an entrepreneurially-minded investor himself, he is embracing new technology and the shifting business landscape to stimulate new market capacity and technically efficient insurance products for the new business era.

Stacey Copeland



Stacey is an account executive with 30 years of experience focused in the resource-based industry in Western Canada. Stacey joined Finning International in 1997 after 7 years at AON, and was quickly promoted to a management position with a mandate to build a highly competitive insurance facility for Finning customers. A combination of high service excellence, successful claims management, and expanded insurance offering meant a fivefold increase in net profitability.

Stacey joined Axis Insurance in 2005 as a senior shareholder and partner, immediately helping the company grow through a series of strategic acquisitions and partnerships and was instrumental in the sale of the company in 2016 to the Vertical Group, now renamed the Axis Group. Although specializing in mining, mineral exploration, forestry and energy sectors, Stacey has expanded her knowledge to include construction, transportation, cryptocurrencies, blockchain and other emerging markets and technology risks.

She aligns herself with clients that are best in class and embraces their technical challenges, meets their high service expectations and considers it the ultimate success to place the broadest coverage, at competitive pricing with A+ rated insurers.