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Insuring Your Property to its Full Replacement Cost

There is an important reason why many insurers are demanding insurance appraisals in order to secure property coverage. This is to ensure that owners are protected in the case of major peril where the property is deemed a total loss.

The full replacement cost, known to appraisers as the Total Insurable Value, is to include the building structure, all common facilities and assets, and any insurable improvements. A professional appraisal should be obtained annually to account for changes to construction costs. Any property owner not obtaining a replacement cost appraisal on a regular basis can be left at significant risk of being underinsured and responsible for any shortfall in coverage.

Annual Updates to Appraisal Amount

Among other things, high demand in the housing market, increasing cost of materials, and Canada's tight labour market all put significant pressure on the construction industry causing it to fluctuate quickly, and often at a higher rate than inflation. It is important that your replacement cost reflects these changes.

Therefore, it is recommended that owners review the adequacy of the insurance annually. This not only ensures that they are always sufficiently covered, but also saves them from paying too much in premiums should there be a dip in industry costs.

It is particularly important to maintain annual updates for phased developments throughout the construction period. Ensuring Total Insurable Value is updated upon the completion of each phase is critical to protecting the development.

This is a Provincial Requirement for Condominiums

Each Condominium Act/Code or Strata Property Act across Canada has a similar bylaw mandating that condo corporations insure their property adequately in the case of a total loss.

The BC Strata Property Act specifies in section 149.1 that the strata corporation must obtain and maintain property insurance for the full replacement value.[i]

In Ontario, the Condominium Act states that the corporation shall obtain and maintain insurance on behalf of the owners for damage caused by major peril, including fire, lightning, smoke and more, and the insurance shall cover the total replacement cost.[ii]

In Alberta, the condo corporation is required to insure the common property and units (not including improvements made to the units by the owners) against loss resulting from destruction or damage caused by any peril, and that this insurance must be equal to the replacement cost of the condominium as described.[iii]

The Civil Code of Quebec stipulates that the syndicate has an insurable interest in the condominium and shall take out insurance against ordinary risks in an amount that is equal to the replacement cost of the condominium.[iv]

The Manitoba Condominium Act takes this a step further, requiring all condominiums to obtain an insurance appraisal before the first unit is occupied and at least every five years after.[v]

Case Studies – The Good, The Bad, and The Ugly

To emphasize the importance of an accurate and up-to-date insurance appraisal, here are three examples of properties that experienced a fire resulting in the total loss of the structure. In the first two case, the condominiums were not adequately covered by their insurance benefit. In the third example, the business had secured sufficient insurance in the amount of the total replacement cost. The results were strikingly different.

1. CHILLIWACK FIRE[vi] – THE UGLY

In August of 2019, a three-alarm blaze tore through an apartment complex in Chilliwack. Investigations determined smoke materials started the fire on a fourth-floor balcony. The fire quickly breached the attic space and by the time fire crews arrived, there were flames as high as 30 feet shooting in the sky.

Fortunately, no one was injured but more than 100 people were displaced in the disaster. To make matters worse, it was determined that the strata was underinsured by a whopping $3.2 million. This meant that each unit owed between $36,000-$57,000 to make up for the shortfall in coverage. Some of the residents claimed not to have personal property insurance, having believed that paying their strata fees would result in the building being appropriately insured.

At this time, whether the fault lies with the strata corporation, the property management firm, or the insurance appraiser, had an appraisal been obtained, is unknown. But what we do know is that many families went without homes for more than two years while the rebuild took place and there were residents who experienced significant financial hardship, not able to pay the assessments or seek legal support.

2. QUEBEC CONDOMINIUM[vii] – THE BAD

In 2008, a condominium was deemed a total loss after a fire destroyed the building. The condo board filed a claim for the common property and the condo owners filed for their personal portions. The corporation did not have sufficient insurance coverage for the common property and there was a $454,938 shortfall. Since the cost of the rebuild was not completely covered by the condominium's insurance, the balance became the responsibility of the unit owners to pay via special assessment, at a cost of $6,119 per unit.

While many of the owners had homeowners' insurance to cover the difference, two owners did not. As a result, these owners were responsible for paying the special assessment themselves. These owners submitted a claim against the condo board and condo management. They claimed that, according to the declaration of co-ownership and section 1073 of the Civil Code of Quebec, it was the responsibility of the condo board to provide insurance coverage for an amount equal to the building's replacement cost, and that the board had failed in their fiduciary duty to do this.

The judge overseeing the case agreed with them and they won. It was determined that neither the board or the manager had acted diligently or prudently in determining a value that was equal to the actual replacement cost value for the building and common property, and they were found jointly liable. Further to this, the manager was found 100% responsible for the damages suffered by the plaintiffs as he had been the one to determine the amount of insurance coverage required on the board's behalf. It was noted that the manager was in a privileged position to know the replacement cost, having been a representative of the developer, but he had mistakenly omitted the taxes from his estimate resulting in the corporation being severely underinsured.

3. ALBERTA MANUFACTURER FIRE – THE GOOD

In 2006, the owners of a manufacturing plant in Alberta obtained an insurance appraisal from Normac on the recommendation from their insurance broker who believed the plant to be underinsured. The owners had been estimating their replacement costs, but had not been updating them on a regular basis with the aid of a professional appraisal. Following Normac's calculation, it was determined that the property had been understating their values by $13 million.

In 2007, one of the main buildings of the plant was destroyed by a massive fire and was also deemed a total loss. Due to Normac's updated appraisal values, the client received full coverage to rebuild the structure and despite this major interruption to their business, the owners were able to thrive in the years following. Thanks to our appraisal which was equal to replacement cost, the plant was properly insured and it saved the owner's business.

Important Points to Remember

When considering these examples, the value of obtaining a proper insurance appraisal is evident. A correctly performed insurance appraisal can save owners millions of dollars in repair and replacement costs and ensures a business can continue to operate after a total loss. Furthermore, working with an experienced appraiser can save owners and boards from significant conflict and protect a condo board or manager from being held liable for a portion of replacement costs.

The most secure way to protect owners and corporations is to obtain an accurate replacement cost for the property annually. Only a professional appraiser can effectively determine the replacement value, which must include demolition and removal expenses, current building practices and technological improvements, local and national bylaw requirements, construction labour and material fluctuations, and necessary taxes.

These true-life case studies underline the importance of always obtaining a current insurance appraisal from a company that specializes in this profession. Disasters do happen, so make sure that your assets are properly appraised.

i. http://www.bclaws.ca/civix/document/id/complete/statreg/98043_09#part9
ii. https://ccitoronto.org/sites/default/uploads/files/condoact1998/CondoAct1998.pdf
iii. https://kings-printer.alberta.ca/documents/Acts/c22.pdf
iv. https://ccq.lexum.com/w/ccq/en#!fragment/sec1072/
v. https://web2.gov.mb.ca/laws/statutes/2011/pdf/c03011.pdf
vi. https://www.cbc.ca/news/canada/british-columbia/condo-insurance-fire-1.5829511
vii. http://www.advantagescondo.com/replacement-value-insurance-policy-the-court-confirms-the-obligation-of-the-syndicate-and-the-administrators-1.aspx

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