

# ADVISER

## IS YOUR PROPERTY UNDERINSURED?

The cost of rebuilding your premises or replacing equipment after a major incident may be more than you think. In fact, Marsh's Valuation Services Practice finds that about 20% of companies that perform regular valuations, or have an indexation scheme in place, are at least significantly underinsured, and about 10% are severely underinsured. These percentages grow to about 60% and 30% for firms that don't regularly review the insurable value of their assets. It is rare that Marsh's team finds that companies are significantly overinsured.

Underinsurance is a critical issue: after a loss it may mean the difference between survival and failure. If you insure for the wrong amount you may not receive the full value of your loss if you have a claim. This is the case even with a partial loss — if the overall sum insured is inadequate, insurers can apply "average". This means they can reduce the claim settlement figure in proportion to the level of under-reported insurance value.

To put the problem in context, if you insured your building for GBP4 million — but it would actually cost GBP5 million to rebuild it — then suffering property damage totalling GBP500,000 could result in your insurer paying you GBP400,000 (less any policy excess). You would have to find the remainder of the money (GBP100,000 and any policy excess) yourself. Because you are 20% underinsured, the claims settlement may be reduced by 20%.

### COMMON CALCULATION ERRORS

- Calculating the sum insured using the original cost, net book value, or acquisition price of the property, rather than the cost of reinstatement.
- Ignoring recent changes like additional buildings and/or machinery.
- Using the wrong rebuilding indices to correct the value of your assets. For example, inflation factors affecting construction costs are sector and geography-specific. General inflation is an incorrect basis but is commonly used.
- Using indices over a long period of time.
- Failing to include items such as the costs of car parks, access roads, perimeter walls, and landscaping.
- Neglecting the allowance made for specialist circumstances, such as:
  - Listed status.
  - Known asbestos.
  - Special constructions.
  - Rare materials used.
  - Lead times for the replacement of specialist machinery.
  - Shortage of replacement machinery.
- Overlooking allowances made for currency fluctuations in respect of specialist equipment that has to be sourced overseas.
- Failing to update sums insured to reflect changes in the business, such as a new acquisition, the development of a new product, or general growth during the year.
- Underestimating the limit needed for extension clauses, such as professional fees and debris removal. Standard provisions of 15% of the sum insured often prove insufficient.

## HOW TO ENSURE YOU HAVE THE RIGHT VALUES

Marsh recommends that you have a professional valuation of buildings and contents carried out every three years. Professional valuers should take account of building materials, increases in labour costs, professional fees, debris removal, and plant hire costs. They will normally advise on the additional provisions necessary to reflect price increases during the rebuild period.

Once a professional valuation has been carried out, buildings, plant, and equipment sums insured can be adjusted annually for inflation by applying one of several indices used by valuers and contractors in the construction industry.

These indices rely on the base figure to which they are applied being accurate and up-to-date. Also, average building costs in most indices cannot accurately reflect variations in different types of structures or detailed geographical variations. Therefore, you may need to use your knowledge of the local labour market and specialist conditions as part of the calculation process.

There are also various cover options available in respect of material damage insurance, which can help to protect you against future inflation costs and the impact on your sums insured. In some instances, we have been able to negotiate policies without an average clause, where clients have had a professional valuation undertaken.

## HOW MARSH CAN HELP

Marsh's valuation experts can provide objective, independent, and fully supported valuations to help organisations procure adequate insurance for their business needs. Our services include replacement cost analysis of buildings and leasehold improvements, contents, machinery, and equipment, as well as other insurable tangible assets.

Marsh can also advise you on alternative cover options for property insurance protection.

Finally, if the worst does occur, our Forensic Accounting and Claims team is on hand to help you calculate and negotiate your insurance claim.

## CONTACT US

For further information and assistance please contact your usual Marsh representative, or email:  
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