Underinsurance
… an ongoing problem for the strata sector.

In spite of the fact that legislation requires Corporations, Owners Corporations, Plans and Strata Companies ("Bodies Corporate") to insure buildings for rebuilding and/or replacement value, it is possible that even with a valuation, the sum insured is incorrect.

Office bearers for Bodies Corporate have substantial obligations and can be held personally liable for their actions and decisions made on behalf of lot owners. In addition, lot owners have an unlimited liability to cover any potential shortfall in insurance funds in the event that a loss is not adequately covered by the sums insured in an insurance policy.

Legislation

In all States and Territories, laws require the Body Corporate to insure buildings for reinstatement and/or replacement value, generally to a condition as new. They also define what property comprises the building, and provide that removal of debris and professional fees need to be taken into account.

In order to ensure a correct valuation, a Body Corporate should engage the services of a suitably qualified and skilled valuer who will correctly calculate the value for insurance purposes, not "market value" as some owners mistakenly do.

Zoning changes

An additional consideration for valuations is the impact of changes to zoning since original build.

Leonie Milonas, State Manager WA for Strata Community Insurance notes, "Many local councils make changes to zoning requirements over time that would have an impact on the cost of reinstatement following a loss".

Consider, for example, a strata building that currently has no dedicated car park, but where council zoning changes require that in the event of a total loss to the building a car park will need to be built. Under this scenario, the building insurance would need to reflect the increased cost of rebuilding and/or replacement associated with the car park to ensure the building is fully covered.

Some other considerations include known hazards (e.g. asbestos material used in roofing), the effect of Goods and Services Tax, and increased costs associated with events of a certain nature – including catastrophes such as earthquakes or cyclones.

Timelines in the Calculation of a Sum Insured

It is vital to ensure escalation of costs has been correctly calculated from the date of the valuation, to the eventual end of the rebuilding/reinstatement period the valuer has considered appropriate for the building in question. The valuer should clearly show the following periods as a minimum, when arriving at the sum insured for rebuilding/replacement:

1. Date of Valuation;
2. Start Date of Period of Insurance;
3. End Date of Period of Insurance, assuming a loss could occur on the last day of the Period of Insurance;

4. Post loss:
   (a) Removal of Debris / Planning period;
   (b) Rebuild period;
   (c) Fit-out and completion;
5. Re-occupation.

Partner for protection

Milonas states “Body Corporate office bearers need to be aware of the implications of underinsurance and their personal liability for decisions made on behalf of lot owners.

They can mitigate this exposure by ensuring they partner with a respected and experienced valuer and have the correct replacement/reinstatement insurance covers in place.”