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Subject: Legislation Update - Insurance Valuations

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All of Your Buildings Must Have an Insurance Valuation by 30 August 2009...

The new Body Corporate and Community Management Regulation 2008 came into effect this Saturday, the 30th of August and between now and the 30th August 2009 you need to ensure that all of your buildings have up-to-date Insurance Valuations.

The Regulation states that, "The body corporate must, at least every 5 years, obtain an independent valuation stating the full replacement value of the building or buildings". This means that if any of your buildings have never had an insurance valuation completed they need to have this done by the 30th August 2009.

Why the sudden need for Insurance Valuation Requirements?

Many Body Corporate Managers already get their Insurance Valuations updated every 2-3 years due to the costs that go into replacing a building. The architecture, labour, building materials and time costs combined with the current uncertain economic state demonstrate the need for Insurance Valuations to cover the costs of building replacement in the event of a disaster.

Recent research shows that some Body Corporate Managers could be looking at a portfolio of buildings underinsured by anything from \$50,000 to \$50,000,000.

What has changed since my last Insurance Valuation?

The Cost of Commodities

Australian commodities continue to sell at record prices. The insatiable appetite of markets like China who are building the equivalent of the whole of Australia's building assets every 18 months keep pressure on the supply side. Basic economic theory dictates that high demand combined with limited supply (constrained by the massive infrastructure needed to increase capacity) inevitably leads to

price pressure.

The recent negotiation of supply contractors by Australia's mining companies again led to massive price rises. Domestically, the price of steel used to reinforce concrete and steel beams and posts has been increasing monthly. This means the maintenance and reconstruction costs of every building in Australia has also increased every month.

And who could forget oil prices! Since doubling in the last two years oil has affected every aspect of supply chain costs from trades people travelling to building sites and steel foundries to the truck that delivers the steel and other supplies to a building.

Trade Skills Shortage

Finding good people in the construction industry is particularly difficult and it has been like this for years now, just talk to anyone in the sector. With the slowdown in new home starts you might expect an easing in demand but activity in other parts of the construction sector has eaten up any unused residential construction capacity. Add together the demands of massive infrastructure projects, a renovation boom, mining boom, all the Aussies in Dubai, dwindling apprenticeship numbers in previous years and you end up with a construction skills crisis.

Not surprisingly demand for trades continues to outrun supply. The table to the right shows the shortage of trades people in Australia and with demand high contractors are charging higher rates for their services. The result of a skills shortage is higher maintenance and construction costs.

Natural Disaster Risk

Apart from this a Body Corporate also needs to look at whether their current valuation would cover the building adequately in the case of a natural disaster. In the event of a cyclone or bushfire, building costs could increase by anything up to 30%.

Trades Availability Mar '05-Mar '08

	Mar '05	Mar '06	Mar '07	Mar '08
Bricklaying	-0.60	-0.26	0.00	-0.27
Carpentry	-0.49	-0.49	-0.30	-0.46
Ceramic Tiling	-0.40	-0.29	-0.36	-0.43
Electrical	-0.38	-0.50	-0.70	-0.25
General Building	-0.48	-0.37	-0.54	-0.44
Joinery	-0.34	-0.63	-0.32	-0.44
Landscaping	-0.30	-0.31	0.00	-0.50
Other Trades	-0.35	-0.42	-0.20	-0.44
Painting	-0.24	-0.24	-0.47	-0.62
Plastering	-0.33	-0.24	-0.29	-0.56
Plumbing	-0.32	-0.42	-0.80	-0.50
Roofing	0.33	-0.10	-0.33	-1.00
Site Preparation	-0.50	-0.38	-0.75	-0.57
All Trades	-0.40	-0.43	-0.41	-0.46

Critical Short Supply is between -2 and -1
Moderate Short Supply is between -1 and 0
In Balance = 0
Moderate Oversupply is between 0 and 1
Massive Oversupply is between 1 and 2

So how does this affect my insurance valuations?

Some Bodies Corporate don't think that being underinsured by a small figure will have that much of an effect on their insurance payouts; but the averaging clause in insurance policies means that insurance claims get paid in proportion to the insured replacement value against the actual replacement cost of the entire building.

For example;

Say one of the buildings you manage was insured for \$2,000,000 but in the event of a total replacement it would cost \$3,000,000 to re-build. Due to the averaging clause you would only receive a payout two-thirds of any claim. So even if the claim was under \$2,000,000; say \$100,000 for flood damage, you would only receive a payout of \$66,666. For a Body Corporate to have to pay the remaining costs of \$33,334 would be a second blow to owners who may have already had to replace their personal belongings after a disaster.

It is essential that Insurance Valuations are constantly updated to ensure that these shortfalls do not eventuate. The new regulations require a valuation to be performed every 5 years. It is widely recommended that they are updated more frequently - at least every 2-3 years if not annually - as even a 5% change in construction costs can have massive financial implications if a total building loss was to occur.

Summary

The economy is constantly changing and construction costs are increasing at well over the rate of inflation. By keeping up to date with Insurance Valuations your Bodies Corporate can feel secure that if a disaster was to occur they would be thoroughly covered.

Regardless all Bodies Corporate need an up to date Insurance Valuation for their next AGM to meet with legislative requirements.

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