

# APPRAISAL RECOMMENDATIONS

## JANUARY 19, 2010

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### EXECUTIVE SUMMARY

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Citizens' goal is to ensure that an appraisal provided to substantiate building limits include an accurate replacement cost valuation ("RCV"). This is imperative for both personal and commercial lines and affects our existing book of business as well as new business. Building limits are based on replacement cost which should be sufficient to rebuild a structure including all materials, features and finishes. This ensures adequate premium is collected for the risk assumed by Citizens and can indemnify the policyholder in case of a loss.

Staff has seen a marked increase in varying quality and completeness of appraisals submitted to Citizens. Since these are relied upon to establish coverage limits and ensure no gaps for policyholders, it is inappropriate to continue accepting the widely varying valuation techniques used by appraisal firms. Common errors and software manipulations consist of:

- Market/loan value appraisals which are not developed for insurance purposes and do not provide the information necessary to confirm the cost to replace the building at the time of loss.
- Building feature line items being adjusted or removed with no explanation, such as walkways, porches, and balconies.
- Unsupported changes in construction quality. The construction quality is generally developed based upon average characteristics for each type of occupancy with "average" defined as the common characteristics of a majority of buildings within that occupancy. Citizens has received multiple 'updated' appraisals where the valuation revises the quality with no explanation. For example, a high-end commercial residential condominium with many custom features had been appraised reflecting a quality rating of '3.0 – Superior' for many years. An appraisal update received in 2009 reflected a quality rating of '2.5 – Average/Good' with no explanation. This change to the quality rating reduced the overall building RCV by millions of dollars.
- Inaccurate occupancy classifications – for example, a commercial residential condominium building using the occupancy code 'condominium shell only' in lieu of 'condominium w/out interior finish'. Using the 'shell only' occupancy would omit major features of the building in the RCV determination such as electrical wiring causing an inaccurate replacement cost valuation.
- Critical data being altered, such as the total square footage of the building or construction type.

To improve the accuracy of building valuations, Citizens must establish a minimum standard for appraisals that requires all appraisals to include specific valuation data and the method used to determine the estimated building replacement cost valuation.

Staff recommends implementing the following minimum requirements for all appraisals submitted to Citizens:

- Appraiser's name and license number, if applicable
- Year built
- Total square footage
- Number of stories
- Construction Type

### **Specific Personal Lines Requirements**

- Appraisals must include an estimate of the replacement cost for every structure to be insured, including ancillary structures.
- The method used to determine the cost of rebuilding the structures must be from a valuation tool designed for insurance replacement cost purposes and be the most current version of the system. The system and version used must be clearly identified. The examples below are two of the most widely accepted programs used in the industry:
  - Marshall & Swift / Boeckh (MSB)
    - ✓ RCT or RCT High Value
    - ✓ Note: When the dwelling exceeds 4,000 square feet of living area or Coverage "A" limit exceeds \$500,000 the RCT High Value must be used
  - E2Value/RS Means
    - ✓ Mainstreet
- High Value homes should include all customized features and materials (e.g., custom countertops, marble tile, etc.).
- Valuation reports must be based on the entire building square footage.
- The construction type used to generate the valuation must be based on the actual ISO construction definitions and the structure(s).

### **Specific Commercial Lines Requirements**

- Appraisals must include an estimate of the replacement cost for every structure to be insured, including ancillary structures.
- The method used to determine the replacement cost valuation must be from a valuation tool designed for insurance replacement cost purposes and be the most current version of the system. The system and version used must be clearly identified. The examples below are two of the most widely accepted programs used in the industry.
  - Marshall & Swift / Boeckh (MSB)
    - ✓ Building Valuation System (BVS)
  - RS Means / E2Value
    - ✓ Pronto

- The “occupancy” used to generate the valuation in the software must be the most accurate selection available as described in the definitions of the occupancy types in the software. (E.g. A residential condo should use the occupancy “Condominium, w/o Interior Finishes” in the MSB BVS software.)
- Valuation reports must be based upon the entire building square footage and include all components of the structure in their entirety (e.g. balconies, walkways, common areas, etc.)
- Construction analysis including construction details for the walls, floors and roof.
- The construction type used to generate the valuation must be based on the actual ISO construction definitions of the structure(s).
- A copy of the system generated report (worksheet) must be included with any appraisal/valuation.
  - The report must be the full detailed report (Summary reports will not be accepted)
  - No adjustments can be made to the architect’s fees, labor & material costs, overhead & profit or construction quality.
  - Any adjustments to individual line items must be done on an addendum to the report and must include a detailed explanation of why the adjustment was made and how the adjusted value was developed.

## **RECOMMENDATION**

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Staff requests that the Committee recommend to the Board of Governors that Citizens implement the appraisal recommendations described above.