REAL ESTATE INSIGHTS

NAVACORD®

Understanding Insurance to Value

Canadians continue to face economic pressures driven by labour shortages, supply chain constraints and an increase in severe weather events. These factors have pushed construction costs higher across the country and increased the financial risk facing commercial property owners.

Statistics Canada reports that non residential building construction costs rose 3.8 percent year over year in the fourth quarter of 2024. While the pace of increases has slowed compared to earlier years, costs remain significantly higher than historical norms. Skilled labour shortages, changes to building codes and volatility in material pricing continue to drive replacement costs upward.

For property owners, these conditions make insurance to value a critical consideration.

WHAT IS INSURANCE TO VALUE

Most commercial property policies insure buildings on a replacement cost basis. Replacement cost refers to the amount required to repair or rebuild property to the same design and quality as before the loss, using current materials and labour and in compliance with current building codes and bylaws. Coverage applies only up to the stated limit of insurance.

Insurance to value means selecting a limit of insurance that fully reflects the building's current replacement cost. When a building is insured to value, the policy can respond as intended following either a partial or total loss.

Problems arise when limits fail to keep pace with rising construction costs. Insurers calculate premiums based on reported values, so under reporting can reduce premiums in the short term. That strategy exposes property owners to potentially significant out of pocket costs if a loss occurs.

SETTING THE RIGHT LIMIT OF INSURANCE

Calculating an accurate replacement cost requires more than estimating the basic cost of reconstruction. A proper valuation includes demolition and debris removal, current labour and material costs, professional fees, permitting costs, compliance with updated building codes and allowances for future inflation.

The most reliable way to ensure adequate coverage is to obtain a professional building appraisal. Industry best practice recommends updating appraisals at least every five years and applying inflationary adjustments to insured values at each annual renewal.

THE IMPACT OF CONSTRUCTION COST INFLATION

Between 2019 and 2024, non residential construction costs in Canada increased by more than 40 percent, according to Statistics Canada building construction price indexes. Even during more stable periods, average annual increases of two to three percent can compound significantly over time.

For example, a building insured for $1 million in 2014 would require a limit closer to $1.3 million to $1.4 million today, depending on location and building type. Without regular adjustments, a property owner may be materially under insured without realizing it.

UNDER INSURANCE AND CO INSURANCE

Under insurance occurs when the policy limit is insufficient to cover the actual cost of repairing or replacing the property. Many commercial property policies also include a co insurance clause, commonly set at 90 percent.

If the insured value falls below that threshold, the insurer may reduce the payout on a partial loss. The payment is calculated based on the proportion between the limit carried and the amount that should have been insured.

For example, if a building's true replacement cost is $1.4 million, a policy with a 90 percent co insurance clause requires a minimum limit of $1.26 million. If the insured limit remains at $1 million and a $500,000 partial loss occurs, the policyholder will recover approximately $357,000 before the deductible. The remaining amount becomes the owner's responsibility.

In the event of a total loss, the insurer would pay the full policy limit, leaving the property owner to fund the uninsured balance.

CONCLUSION

Construction costs continue to evolve, even as inflation stabilizes. Regular appraisals and annual insurance reviews help ensure coverage reflects current rebuilding costs. Working with a licensed appraiser and an insurance broker allows property owners to adjust limits proactively rather than discovering a shortfall after a loss.

In today's construction environment, insurance to value remains essential. It plays a critical role in protecting the long term financial stability of commercial properties across Canada.

If you have questions specific to your business, or would like additional information, please reach out to your Navacord Insurance Services Alberta Inc. Advisor.

LET US HELP YOU MANAGE YOUR RISK

9 Office Locations
Across Alberta and Interior BC

lloydsadd.com
AB.info@navacord.com