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## Depreciation/Holdback - Understanding this Property Insurance "Cost Driver"

The replacement cost provision in your property policy for building and personal property coverage took an about face with the passage of the most recent property insurance legislation in 2011. As previously written, due to the dissatisfaction and outcry by policyholders after the 2004/05 hurricanes, the legislature required insurance companies to pay the full "replacement cost" of your loss up-front with no depreciation/holdback of your money. This legislation only applied to "admitted" insurance carriers in the personal lines market. Subsequently, the lobbyists for the insurance companies said this legislation was over generous to the policyholder and this largeness became what is now known as a huge "cost driver" for the insurance industry.

So going forward, you will be paid the "Actual Cash Value" (ACV) of your loss which means depreciation/holdback will be withheld from the first payment following your loss. Given the likelihood that recovering this portion of your loss will (in our opinion) be problematic and challenging, we think you should be as informed about this process as the adjusters who are sent out by the insurance companies.

Depreciation or holdback is money that will be held by your insurance company until you can prove you have spent your claim money for the full replacement cost of your loss which in the case of a hurricane loss will require you to be out-of-pocket for the deductible percentage as well. The good news is that you have the ability to argue a lesser depreciation/holdback percentage in the event you disagree with the insurance adjuster's "opinion" of

the value of your property.

What does the actual cash value of your loss mean and how can you empower yourself to deal with an adjuster who may be overly aggressive applying depreciation or holdback to your claim payment? First, look for the definition of "Actual Cash Value" in your insurance policy. Our experience has been that most property policies do not define the term "Actual Cash Value," "Depreciation" or "Holdback." If it's not defined, then how is a fair depreciation/holdback amount arrived at?

An online search for the term "Actual Cash Value" will result in all sorts of information and opinions that attempt to explain the process to calculate the ACV of a loss. So which one is right, and do you, the policyholder, have a say in how much you will be penalized with depreciation?

Take for example the definition found in a real property appraisal that was commissioned to assist the client with the determination of the proper amount of insurance coverage limits to carry on a condo association for insurance valuation. In this appraisal, depreciation was defined as "the loss in value due to deterioration caused by usage, wear and tear, and the elements." The appraiser who authored the report took 34% depreciation on the buildings, yet nowhere in this report is there any methodology as to how this percentage was arrived at. So clearly if depreciation is not defined, it is at best an art, and at worst a guess and in the eyes of the beholder.

Insurance companies will often teach a simple mathematical formula to determine depreciation based on some in-house life expectancy tables that are at best subjective. Applying a ratio to the age of an item over its purported life expectancy will equal a percentage to be applied against the replacement cost of an item. Many would argue the fairness of this method depends on whose life expectancy tables are being used. This method certainly does not take into consideration usage or the care one owner may take versus another. One would expect a household with many family members to likely have more wear and tear on personal property and structure than a retired couple or a single person having the same home and contents purchased within a similar time period. This same concept applies to building losses. A well maintained building with scheduled maintenance and repairs performed as required should not fall victim to some arbitrary and draconian depreciation tables. Given this ambiguity, some states including Florida follow what is referred to as the "broad evidence rule" which in

simple terms means any and all things could be used to determine the fair market or actual cash value of an item or structure. Only you, the policyholder, know the true condition of your property prior to its loss based on its usage, wear and tear, or lack thereof. You are also aware of the quality of an item which will play a part in its useful life.

The main message here is not to hesitate to challenge the value and depreciation applied to your claim. Every dollar you reduce depreciation/holdback is a dollar in your pocket. If you disagree with the adjuster's depreciation opinion and the amount they are holding back, gather your facts and present the information to your insurance company. Know the rules and know that the fair amount of depreciation to be taken can be subjective and subject to negotiations.

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