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HOW IS THE INSURED VALUE OF A PROPERTY CALCULATED?

In the course of purchasing a property and obtaining a mortgage loan from a bank, the purchaser often notices that the bank requires the property to be insured for an amount that is higher than the actual value of the property. In order to understand why the sum insured amount is higher than the value, one must understand what property insurance actually entails.

Homeowners' Insurance (or HOC as it is often referred to) covers all of the structures on a property. It covers the electrical system, the plumbing, the house itself, the roof, and numerous other things. Therefore, the property must be insured for an amount that would be enough to rebuild the property, the replacement value, in the event of an insurable event occurring, and not the market value. The cost of rebuilding necessarily includes the removal of rubble, the drawing of plans and other legal requirements. Indemnity insurance also works on a "new for old basis", meaning that the materials that will be used to rebuild the property, will be more expensive than the materials that were used to initially build the property.

Insurance Companies and Banks use complex mathematics to determine the actual sum insured amount of the property, which includes various factors such as the area where the property is located and the age of the property. For example, if Property A is situated in Waterkloof, the sum insured value will be higher than if that exact same property was located in Cullinan.

As a general guide, a property will be insured for 125% of the value so as to ensure that the cover is adequate to pay for all the expenses associated with rebuilding the property.