# *Burand's Insurance Agency Adviser*

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## Would you like to make an impact and help raise the bar?

I'm not sure who will win the race to the bottom because there are too many contestants. The plaintiff attorneys have a point in many of their cases because incompetence, combined with questionable dealings, results in signs stating, "Sue me!" Agencies and carriers might as well get the signs preprinted.

But judges are complicit. A recent property case resulted in the judge allowing the carrier to use "New" Construction replacement cost to be used on a partial loss versus the "Remodel" or "Repair" construction cost. Everyone knows that repairing a building costs more for the same work than building new. The judge ruled the policy did not dictate the replacement cost model to be used. So much for ambiguous language always working in the insured's favor for all the amateur agents advising clients as such.

A second ruling that could not be more wrong ruled in favor of the agency in an E&O case. The agency advised the client they had coverage (they didn't), did not provide the client with a copy of the policy so that the client could fulfill their "responsibility to read and understand" (a silly standard), advised the client to not turn the claim in immediately, suggested the claim was covered (agents have zero authority to tell clients claims are or are not covered), and still won the suit! I won't pretend to understand the legal technicalities that may have enabled the agency to win. The agency was extremely lucky the carrier did not pay the claim and then sue the agent. I think the carrier would have hired a better attorney than the insured hired.

These situations are ruining the industry. Worse, it makes competing against carriers playing games with claims and agents that, while I'm sure the agent in the above case meant well, did just about everything wrong based on how I read the court ruling.

This is the inevitable course in all industries, as first modeled by the great economist Carl Shapiro in his theory of mediocrity. Every industry will suffer from people cutting corners in ways consumers do not discover until after the fact. The ONLY solution is to create a separate class with true professional designations. This is not my idea. He spelled out the solution in 1985. I'm only applying this to insurance distribution.

If you want to be part of a founding program for true professionalism and are willing to spend the time and money, contact me. Let's try to make a difference for the benefit of consumers within the industry rather than giving this ground to plaintiff attorneys and consumer advocacy groups.

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# The Importance of Hiring a Qualified Appraiser

A recent IRS case highlighted the importance of hiring a qualified appraiser for asset and business transactions. "Qualified" is a definition provided by the IRS. A person cannot legitimately claim to be "Qualified" if they don't meet the definition provided by the IRS.

Here is an AI summary, which is actually a pretty good summary of the situation. The Hidden Risk of Using Unqualified Business Appraisers:

Choosing a business valuation provider based solely on price can be a costly mistake. Appraisers who lack recognized credentials or fail to follow professional standards may deliver reports that look polished but are fundamentally flawed. Here's why it matters:

- Regulatory and legal risk: The IRS requires business valuations for tax purposes to follow recognized standards (Rev. Rul. 59-60, Publication 561). Reports by unqualified appraisers can trigger audits and tax penalties or be rejected outright.

- In litigation, expert valuations must meet the Daubert standard. Courts regularly exclude non-compliant or non-credentialed valuation reports.

- Professional standards exist for a reason. Organizations like NACVA, ASA, and AICPA set professional standards (e.g., USPAP, SSVS1) that ensure valuation reports are consistent, reliable, and defensible. Reports that deviate from these standards can contain material misstatements or unsupported conclusions, which can lead to financial harm or liability.

How to Identify a Qualified Appraiser:

- Look for credentials from NACVA (e.g., CVA), ASA, or AICPA (e.g., ABV).

- Ask if the report complies with USPAP and SSVS1 standards (VERY IMPORTANT).

- Ensure the appraiser has experience with your type and size of business.

- Further Reading and References:

- IRS Publication 561: [https://www.irs.gov/publications/p561](https://www.irs.gov/publications/p561)

- NACVA Standards and Ethics: [https://www.nacva.com/page/standards_overview](https://www.nacva.com/page/standards_overview)

- Business Valuation Resources: [https://www.bvresources.com/](https://www.bvresources.com/)

- ASA Business Valuation Standards: [https://www.appraisers.org/Disciplines/Business-Valuation](https://www.appraisers.org/Disciplines/Business-Valuation)

Real-world consequences exist for failure to use a qualified appraiser who not only arrives at a reasonable number but also writes the report in the correct format. Many appraisers offer cut-rate appraisals because their reports do not meet the required parameters. Look for phrases like “Indication of Value” to identify situations where the report probably will not meet the required standard.

If you do not want to take my word for this, here are some court cases for your reading pleasure:

- In Estate of Gallagher v. Commissioner (T.C. Memo 2011-148), the Tax Court rejected an appraisal for methodological flaws and lack of reliable inputs.

- Estate of Scott M. Hoensheid v. Commissioner (T.C. Memo 2023-34). In this 2023 Tax Court case, the estate utilized an investment banker, who lacked formal appraisal credentials, to value closely held stock for a charitable donation. The court determined that the individual did not meet the IRS’s definition of a “qualified appraiser,” leading to the disallowance of the charitable deduction. The court emphasized that "mere familiarity with the type of property being valued does not by itself make [someone] qualified."

- Appraiser disqualified for contingent fee arrangement: In a Colorado case, the appraiser was disqualified after the court found his fee was contingent upon the appraisal outcome, a direct violation of impartiality standards. The court concluded that his financial interest compromised the appraisal's fairness and credibility, rendering the valuation inadmissible.
- Connelly v. United States (2021). In this case, a buy-sell agreement lacked specific qualifications for appraisers, merely requiring five years of experience in appraising similar businesses. The absence of mandates for formal education or recognized valuation credentials led to concerns about the credibility of potential appraisals under the agreement. This underscores the importance of clearly defining appraiser qualifications to ensure reliable valuations.
- Miller Kaplan: "Risks of Unqualified Appraisers". An article by Miller Kaplan highlighted a scenario where a novice appraiser used outdated data spanning two decades to value an event planning company. This approach failed to account for significant industry changes, such as the impact of the COVID-19 pandemic, leading to a flawed valuation. The case exemplifies how a lack of current industry knowledge and proper methodology by unqualified appraisers can result in inaccurate valuations.

To meet IRS requirements, the appraiser must meet the IRS's definition of "Qualified." The report must meet the applicable standard. The methods used must be recognized.

Hiring a cut-rate appraiser may save upfront money, and if you don't get caught, you might be fine. However, a poor report can derail business sales, financing, estate planning, and dispute resolution. And believe me, if a dispute arises involving a poorly written report and the other side has a good expert, you will lose.

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# What is Replacement Cost?

Every good insurance professional strives to convince clients to insure their homes and buildings to full replacement cost unless extenuating circumstances exist. They do this because full replacement cost is the best method for protecting clients. If their home or commercial building is lost and they have full replacement cost, they can rebuild their buildings and lives much more quickly, with much less stress. A professional insurance agent's goal is to provide the best coverage for the worst event.

Losing a home or commercial building only to learn that you are underinsured and you cannot rebuild without taking on a new mortgage, while still having to pay off the old mortgage or having to take out retirement savings, can be financially and emotionally devastating. According to several estimates, a large percentage of properties are materially underinsured.

Underinsuring property does not benefit the agent. Underinsuring property means lower commissions for the same amount of work and a higher probability of being sued. It makes no sense to underinsure property unless you are one of those agents who underinsure so that you can trick a client into thinking they're saving money. And I've been writing long enough to know some readers who don't think this happens purposely. Not only does it happen, some carriers have been known to train agents to sell like this. They should lose their license. Period.

Carriers should not want to underinsure because they lose premiums for only a partially reduced exposure profile. They risk brand injury when claims are not paid. And they make more work for their agents. Two exceptions exist here. The first is they have nothing to sell but price, so they encourage reducing coverage to pretend their rate is better. The second is some carriers likely have a TIV issue overall or in certain geographic areas.

Another reason is less purposeful, and that is through incompetence and ignorance. This begins with replacement cost estimators. The margin of error on these is so high that, at best, the results should be considered ballpark, and the ballpark is the size of several baseball fields. Back when replacement cost was first calculated, carriers recognized that, lacking data and technology, the error rate would be high, so they began offering guaranteed replacement cost. Initially, many of these endorsements were unlimited and not heavily dependent on a precise replacement cost calculation. Over time, though, most carriers began stipulating that for the guaranteed replacement cost coverage to be triggered, the building had to be insured within X% of the replacement cost at the time of the claim, and furthermore, the guaranty was only good for Y% more than the stated coverage amount. If the estimators were better, these limitations would not be an issue, but the estimators are not better.

The high error rate is due to many factors, often all playing a part:

**User error.** The providers of these estimators need to provide considerably more training on how to use them, and the users need to better articulate to clients how to describe their building, better measures, and so forth. Several years ago, I tested my own home. The variance was almost 75%, depending on the estimator used and the agent using the estimator. That variance is so high it's worthless.

A good place to begin is with quality definitions, maybe even standardize the definitions. What is a normal cabinet versus a custom cabinet? If I go to a big box store, cabinets are all pretty normal to me, not custom in any way, and yet the price differs significantly. The same goes for trim, appliances, and even paint. I can increase the replacement cost of a house by at least 25% on this basis alone.

**Carriers insisting on fantasy values.** I don't know where some carriers are getting their estimates. I saw an estimator for Hawaii that, by square foot, was the same replacement cost as Arizona. It is as if the carrier never looked at a map to learn that around 90% of the materials must be shipped to Hawaii, and container ships are not free. Completely inexplicable.

This is an easy example for everyone to comprehend. This happens a lot in the real world, not just in Alaska and Hawaii. I want to believe carriers are just far behind times, and their obstinate refusal to insure to value is not because they have a TIV issue they don't want to admit. The first step to recovery is admitting you have a problem.

**Improved Terminology.** With such high error rates, carriers and regulators should consider better terminology to suggest that replacement cost is a good faith guess. Doing so might minimize disappointment upon learning a home is not insured to value post fire.

Furthermore, a huge portion of homes and commercial properties today are not insured to true replacement cost because the standard policy does not include adequate ordinance coverage. Suppose a home is lucky enough to be insured to value and the guaranteed replacement cost endorsement kicks in, but then major upgrades are required to meet ordinance requirements. In that case, the insured will unhappily discover they're still materially underinsured. Replacement cost only applies to how it was, not how it must be. Real world matters.

Better terminology would help everyone understand what is being insured, so consumers would be less likely to think they have adequate coverage when they probably don't.

**Now, for the egregiously wrong part of replacement cost: Some carriers are effectively doing a bait and switch**. In a March 30, 2025 blog by Chip Merlin of Merlin Law (I highly recommend subscribing), he wrote about a recent court ruling that allowed a carrier to use software to calculate the cost of rebuilding. One problem is that this software is not the same software used to calculate replacement cost in the first place. That makes no good sense.

But worse, the software, by everyone's agreement apparently, calculates replacement cost as if all rebuilds were new construction even if it was restoration/remodel, i.e., a partial loss. Restoration often costs materially more than new construction, so why would a carrier be allowed to only pay for the claim based on a "new" construction estimate versus the reality of a restoration estimate?

The carrier in the case said its policies do not require the carrier "to use any specific estimating methodology." I guess they put a thumb in the air then. I have never worked with this carrier or had clients who did, so I do not know how they manage their replacement cost estimators upon application. But many policies do not define adjusting methodology.

This is a bait and switch. If a method must be used to calculate replacement cost, the same method should be used to calculate the claim. And if the numbers are low even on a new construction basis, then know that replacement cost will be especially low on a partial loss, which increases the need to increase coverage values.

This thought process begs bad publicity, bad faith, and more litigation. Pinching dimes to save pennies makes no sense. I wonder if the added litigation costs are being compared to the savings from clients who don't sue?

This particular carrier's five-year homeowners loss ratio is so bad, they may be getting desperate if I'm guessing correctly. But a loss ratio that high suggests a better solution exists, including smarter underwriting management and maybe doing a better job calculating replacement costs upfront (more premium and about the same losses) versus using what I consider inappropriate claims calculating software.

Professional agents can help protect clients by learning the ins and outs of replacement cost estimators and policy provisions. Then, ask the questions this legal case poses: "What method do you, the carrier, use to settle property claims? Do you use the same calculation method to settle a claim as you do to estimate the original replacement cost? How about partial claims?"

And better yet, fire the carriers that play these games. Don't write with them.

Fair, ethical claims adjusting pays dividends, including maybe elevating an awful reputation to a slightly less awful reputation. Nothing good comes from the lack of transparency in these situations unless a person/company has something to hide and then gets away with hiding it. If a carrier says their rates are based on this trickery, we are just back to the carriers who might still be teaching agents to sell inadequate coverage and pretending it is adequate, but cheaper.

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**Chris Burand** is president and owner of Burand & Associates, LLC, a management consulting firm that has been specializing in the property/casualty insurance industry since 1992. Burand is recognized as a leading consultant for agency valuations and helping agents increase profits and reduce the cost of sales. His services include: agency valuations/due diligence, producer compensation plans, expert witness services, E&O carrier approved E&O procedure reviews, and agency operation enhancement reviews. He also provides the acclaimed Contingency Contract Analysis® Service and has the largest database and knowledge of contingency contracts in the insurance industry.

Burand has more than 35 years' experience in the insurance industry. He is a featured speaker across the continent at more than 300 conventions and educational programs. He has written for numerous industry publications including the Insurance Journal, American Agent & Broker, and National Underwriter. He also publishes Burand's Insurance Agency Adviser for independent insurance agents.

Burand is a member of NACVA, a department head for the Independent Insurance Agents and Brokers of America's Virtual University, an instructor for Insurance Journal's Academy of Insurance, and a volunteer counselor for the Small Business Administration's SCORE program. Chris Burand is also a Certified Business Appraiser and certified E&O Auditor.

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Burand & Associates, LLC is an advocate of agencies which constructively manage and improve their contingency contracts by learning how to negotiate and use their contingency contracts more effectively. We maintain that agents can achieve considerably better results without ever taking actions that are detrimental or disadvantageous to the insureds. We have never and would not ever recommend an agent or agency implement a policy or otherwise advocate increasing its contingency income ahead of the insureds' interests.



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