

Insuring Your Commercial Property During a Vacancy

Commercial property owners are struggling to balance a positive bottom line as tenant vacancies and insurance premiums increase.

According to Moody's Analytics' Q4 2023 Preliminary Trend Announcement, commercial real estate is in limbo. Their analysis revealed the following trends:

- Multifamily, office and industrial spaces declined in rentals and sales
- High interest rates squeezed funding and refinancing risks
- Climbing insurance costs cut into operating income for many commercial properties

In response to market fluctuations, some property owners have reduced their coverage to save money. But this strategy isn't always the best way to go, even if it saves some cash at the outset. You could end up paying far more than you save in the long run.

Instead of cutting your coverage, ask your independent broker for a policy review. Start by clarifying the language in your commercial property policy and comparing it to your current situation. Evaluate your coverage limits and understand your policy definitions, including vacancy clauses.

YOUR POLICY'S VACANCY CLAUSE AND DEFINITIONS

Vacancy clauses exist because commercial properties have an increased risk of damage or loss from things like theft, vandalism and weather damage. If an insurance company insures you when your building is fully occupied, a lower loss rate is applied. If you lose occupants, the chance of property loss increases. Insurance companies build the possibility of a vacancy into their policy terms, which offsets their liability and transfers it back to you.

Check the definitions section of your policy. Look for what your insurance company considers a "vacant" or "unoccupied" property.

Vacancy clauses automatically affect your coverage and payouts

- Most policies require you to rent or occupy 31% or more of the total square footage of your building. (Buildings under construction or renovation are not considered vacant, but you must alert your broker.)
- Policies put a time limit on what they consider a vacancy, usually 60 consecutive days. After 60 days, your insurance won't cover certain types of damage or pay out at the same rate. Standard policies might reduce the payout by 15% or more, depending on the insurance company.
- A policy might automatically downgrade coverage from replacement cost to actual cash value, creating a significant coverage gap.

Interpretation of these clauses can vary and become a point for litigation. Your broker can help you understand your policy's language. They can also explain different situations that would require a change in coverage or special endorsement.

MAINTAIN YOUR GENERAL LIABILITY COVERAGE

Even if your building is vacant, you'll still need general liability insurance if someone gets injured on your property. Empty buildings can attract kids and squatters. You could be held accountable for their injuries, even if they were trespassing.

BRIDGE THE VACANCY GAP WITH ENDORSEMENTS

Tell your broker immediately if you know your property is or will become vacant. They can add coverage to bridge the gap with endorsements like:

- **Vacancy permit coverage:** allows your property to remain vacant for an extended period and still be covered under the insurance policy.
- **Building glass coverage:** helps with the costs of replacing windows and other glass on your property.
- **Vandalism and malicious mischief coverage:** protects against damage caused by vandalism.
- **Replacement cost coverage:** guarantees the insurance company will pay the full cost to repair or replace damaged property without accounting for depreciation.
- **Water damage legal liability coverage:** kicks in if an adjacent property is damaged by water from your vacant property.

FIND WAYS TO KEEP YOUR PROPERTY OCCUPIED

Beyond insurance, there are other risk management strategies that property owners can use to handle vacancies:

- Install security cameras.
- Hire security.
- Maintain your property.
- Lease to pop-up stores.
- Transform the property into a shared space.

CALL YOUR BROKER IF YOU HAVE A VACANCY

Vacancy clauses can create costly coverage gaps. Your broker can help you determine if you're within your policy's occupancy thresholds. If you aren't, they can help you secure the right endorsements to avoid expensive exclusions.

If you have questions specific to your business, or would like additional information, please reach out to your Waypoint Advisor.

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30+ Locations
British Columbia, Canada

waypoint.ca
info@waypoint.ca
866.674.2816

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