VALUATION CASE STUDY
IN THE BLEAK MIDWINTER

The Challenge

During the brief summer months, streams gurgle happily down mountain sides to the sea, waiting below. In winter, gales hurtle across the Gulf of St. Lawrence to vent their fury at the great land mass that seeks to block their way. This is Gros Morne National Park, an area of outstanding natural beauty on Newfoundland's west coast. The Vikings settled here, some 300 kms to the north at L'Anse aux Meadows, over 1,000 years ago. More recently the area has been sparsely populated along the road that hugs the coast. A modern resort complex, golf course, RV park and gas bar attempt to capture trade from visitors attracted to this picturesque region. In 2008 a road side motel was extensively renovated and expanded to include 20 luxury suites, fine dining restaurant, meeting and banquet facilities. The owner reportedly invested $20 million in the resort development. However it struggled to get established and its dream of becoming a landmark and significant employer remained unfulfilled. In December 2011, five short days before Christmas, the main building was destroyed by fire. It was not going to be rebuilt: how should the fire insurance claim be calculated?

Turner Drake's Approach

When a building is destroyed, compensation under the fire insurance policy is normally based on the cost to rectify the damage . . . provided that the building will be reconstructed in a similar manner to the original. However if there is no intention to rebuild, insurance policies normally mandate that the loss be based on Actual Cash Value (ACV) rather than Replacement Cost New (RCN). Actual Cash Value is generally synonymous with Market Value though the courts differ in their view as to how it should be calculated. Defining Actual Cash Value is therefore analogous to nailing jelly to a wall. In essence the governing principle is that the insured be fairly compensated for their loss. Often this can be accomplished by calculating the Replacement Cost New (RCN) and deducting therefrom the Physical Depreciation i.e. wear and tear. This is most often the course adopted by the courts. However it obviously overstates the loss when the property is over built i.e. constructed for a demand that does not exist . . . and such was the case here. The Market Value of the destroyed building would have to be measured by first computing the property's value before the fire and deducting therefrom the value of the land. The Income Approach is the primary method for estimating Market Value for this type of property so we analysed its operating revenue and expense history, researched tourist statistics and trends, identified and quantified competitors within its market segment. We also researched and analysed available sales data for similar type properties in order to utilise the Direct Comparison Approach to validate our estimate of Market Value.

Winning Results

The fire insurance claim was settled without the necessity for arbitration, based on our computation of Market Value.

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