



COMMONWEALTH OF PUERTO RICO  
OFFICE OF THE COMMISSIONER OF INSURANCE

August 21, 2006

RULING LETTER NO.: N-AP-8-75-2006

TO ALL DOMESTIC INSURERS, GENERAL AGENTS, AND MANAGERS OF  
FOREIGN INSURERS AUTHORIZED TO UNDERWRITE PROPERTY  
INSURANCE IN PUERTO RICO, AND TO ALL PRODUCERS AND RATING  
ORGANIZATIONS

**PROPERTY POLICIES FOR CONDOMINIUMS AND FOR APARTMENTS  
IN CONDOMINIUMS**

Dear Sirs and Madams:

The Office of the Commissioner of Insurance (OCI) has learned that, on mortgage loans related to the financing of apartments in condominiums, the mortgage institutions have required that the titleholder obtain an additional property policy to cover the apartment structure because they understand that the limit of the master policy is inadequate. In accordance with the information with which we have been provided, said requirement is a demand of the investors in the secondary mortgage market to adequately insure their investment.

Regarding this requirement of the mortgage institutions, it is important to establish that Article 27.160(7) of the Puerto Rico Insurance Code, Public Law No. 77, enacted on June 19, 1957, as amended, prohibits that a person demand as a condition for granting a finance contract, that additional insurance be obtained on a property that is already duly insured for said risks. To these effects, Article 27.160, as pertinent, provides the following:

"No person shall require, as a condition for a loan or the purchase or deposit of property pursuant to a contract, or in connection therewith, that a property which is otherwise insured by property insurance up to the total value thereof, or

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said insurance is required for the total value thereof, has to be newly covered by other property insurance with the same risks, whether with the same insurer or not and whether for the same limits or not."

However, this same article acknowledges that the aforementioned does not constitute an impediment for the lender to exercise the right to demand that the property be insured for the limits the lender deems most appropriate. In light of this provision, and in order to equally protect the interests of all parties involved in this transaction, the OCI, by means of this document, has established the following parameters that must be satisfied when insuring the risks of condominiums and apartments in condominiums:

### I. Master Policy of the Condominium

1. The maximum limit that the mortgagor may require under the property policy that covers direct damages to the property financed by the mortgagee is the **replacement value** of said property. In the specific cases of condominiums, the maximum limit that may be required under the master policy of the condominium is the replacement value of the common elements of the condominium plus the replacement value of those other elements that, in accordance with the master policy, the statutes of the condominium, or the determinations of those who represent the majority of the titleholders, shall be insured by the Condominium Association. This means that it shall be clearly determined whether, in addition to the common elements, as defined by the Horizontal Property Act, Public Law No. 104 of June 25, 1958, as amended, certain elements will be covered under the master policy of the condominium as they were originally built or installed, such as, but without being limited to: **non** load-bearing walls, doors located in the interior of the apartments, kitchen cabinets, parts that compose the bathrooms inside the apartments, and accessories fixed on the structure inside the apartments. These elements shall be from hereon referred to as "Original privative elements, adhered to the structure."
2. To determine the aforementioned replacement value it is necessary to have a **valuation of the condominium**. A valuation provides the replacement value, that is, the reconstruction cost, and is **not** the sale value of a property, which considers other factors such as location and view, which are not relevant for the purposes of property insurance. In those cases where an appraisal is requested or available, for the purposes of the insurance to be acquired, all the parties involved in the transaction shall make sure that they use the replacement value and not the sale value of both the property and the elements to be insured.

The valuation must be included in a report that itemizes in detail the elements of the condominium considered in such valuation with their corresponding values, in such a way that the insurance producer may offer adequate guidance to his or her client regarding the insurance limits to be acquired, based on the replacement value of all the elements that will be insured under the master policy, as determined<sup>1</sup>. The valuation report shall be prepared by a recognized professional, whether a natural or legal person, specializing in such labor<sup>2</sup>. Unless extraordinary circumstances that destabilize the market arise, the OCI shall consider the valuation of the condominium to be adequate for a term of two years.<sup>3</sup> The Condominium Association of each condominium shall be the custodian of the valuation report and it shall be available to any titleholder or any person interested in acquiring an apartment in the condominium.

3. If an adequate valuation that provides the replacement value of the condominium does not exist, the designated insurance producer shall process, in the name of the insurer who will issue the master policy, the valuation of the condominium in order to adequately fulfill the duties imposed on him or her by Article 9.022 of the Insurance Code of Puerto Rico, of " providing the consumer with a clear and complete orientation about the coverage and limitations of the insurance, and identify and measure the possibility of loss." For this reason, in cases where there is no adequate valuation of the condominium, for those master policies that become effective on or after September 15, 2006, the designated producer shall process such valuation before placing the policy.

Likewise, the producer is required to confirm in writing the elements that shall be insured in accordance with the request of the Condominium Association. We hereby reiterate that the limit of the master policy shall depend on the property and the elements that are to be covered in accordance with the determination of the Condominium Association. We hereby clarify that under every policy in effect before September 15, 2006 all the original private elements adhered to the structure shall be considered covered until the renewal of these policies or until their anniversary, if the appropriate valuation is carried out on the anniversary. This presumption of coverage shall operate unless it is proven with authentic evidence that there was a conscious decision of the

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<sup>1</sup> As explained before, this determination is the one that is made in accordance with the master title, the statutes of the condominium or the determinations of those who represent the majority of the titleholders.

<sup>2</sup> In the case of an appraiser, he or she shall be duly authorized to make this type of valuation.

<sup>3</sup> A master policy that is issued for the limits of the replacement value provided in the valuation, during this term shall be considered as having adequate limits until the expiration of said policy.

Condominium Association that such elements would not be covered in the master policy.

4. You are hereby reminded that in accordance with the provisions of Article 27.081 (5) of the Insurance Code of Puerto Rico and Ruling Letter No. N-AM-10-120-2000 of October 30, 2000, every insurer must offer the option of a clause for a deductible prorated in percentage terms for every property policy that covers a condominium. As established in subsection six of the aforementioned ruling letter, by "offering" we understand informing the insured or proposed insured about the right that the Law provides him or her to include in their policy a clause for a deductible prorated in percentage terms, and grant that option, if it is so required by said insured or proposed insured<sup>4</sup>.

## **II. Additional policy available to the titleholders of apartments to insure items not covered by the master policy.**

1. **Policy to cover the original private elements attached to the structure and their alterations and improvements; either one or both.** If the master policy is acquired for the replacement value of the condominium, but does not provide coverage for the original private elements adhered to the structure, these can be insured by the titleholder of each of the apartments, through a policy issued in his or her name covering said property. To determine the limit of this coverage, the percentage of participation of the specific apartment, as established in the master title, shall be multiplied by the total replacement value of the original private elements adhered to the structure<sup>5</sup>, as established in the valuation of the condominium.

If **alterations and improvements** to the original private elements adhered to the structure have been made in the apartment, these could also be insured through a policy issued in the name of the titleholder<sup>6</sup>. In those cases where the apartment is financed, the mortgage institution shall

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<sup>4</sup> For your convenience, we have included as Annex A to this Ruling Letter, the Notice to the Condominium Association which in accordance with Ruling Letter No. N-AM-10-120-2000, supra, shall be provided to authorized representatives of all the insured or possible insured condominiums before the issuance of a renewal or a new policy.

<sup>5</sup> Elements not included in the master policy coverage. For applying this formula, the replacement value mentioned is the total value of said elements in all apartments.

<sup>6</sup> This policy shall be the same policy to cover the original private elements adhered to the structure, if the decision was not to cover them under the master policy.

coincide with the mortgagor regarding the replacement value of the alterations and improvements<sup>7</sup>.

In those cases where the intention is to insure both the original private elements adhered to the structure and the alterations and improvements, the limit of the policy shall consist of the sum of the replacement value of these two items.

**2. Policy to cover in excess of the master policy of the condominium when it has been acquired for a limit that is lower than the replacement value of the condominium.**

If this situation occurs, which should happen as an exception, the maximum limit eligible by the mortgage institution under the policy that covers in excess for each apartment shall be the participation corresponding to the apartment of the amount not covered by the master policy of the replacement value of the condominium after having applied the percent of coinsurance under this policy.

- a) In addition to the master policy of the condominium, only a policy that provides structure coverage for a specific apartment can exist or be issued. Therefore, the coverage in excess of the master policy of the condominium shall be provided under the same policy issued in the name of the titleholder, as mentioned in the previous subsection one.
- b) No coinsurance clause shall apply under any property policy, issued or to be issued, that provides structure coverage for an apartment in excess of the coverage provided by the master policy of the condominium. Considering that this policy supplements the master policy of the condominium, and does not insure the apartment for the total replacement value, it is not legitimate to apply the coinsurance clause.
- c) When policies for apartments are issued in excess of the master policy of the condominium under the Housing Program<sup>8</sup>, the use of endorsement DP Exceso 08 06 PRS, included as annex B of this ruling letter, is required. On the other hand, if said policy is issued under the Residence Owners Program (HO-6), the use of endorsement HO

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<sup>7</sup> This value is the reconstruction cost and shall not be affected by other factors that are considered when the sale value of an apartment is determined.

<sup>8</sup> One of the Housing Forms with endorsement DP 17 66 07 88.

Exceso 08 06 PRS (included as annex C)<sup>9</sup> is required. This requirement applies to those policies, new or renewals, which are issued on or after September 15, 2006. When placing one of these policies, the insurance producer will provide orientation to the apartment titleholder regarding the type and the scope of the covers provided<sup>10</sup>.

Strict compliance with the provisions of this ruling letter is required from all entities transacting property insurance for condominiums and apartments in condominiums.

Very truly yours,

SIGNED

Dorelisse Juarbe-Jiménez  
Commissioner of Insurance

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<sup>9</sup> The insurer shall consult with the OCI regarding any other product that was previously approved by the Office that is used to provide the excess cover.

<sup>10</sup> The insurance producer shall provide orientation to its client or possible client, among other extremes, about the following: whether the coverage is based on specific risks or for every risk that is not excluded, and whether payment in case of loss will be based on the real value in the market (Form DP 00 01 07 88 with endorsement DP 17 66 07 88) or based on the replacement cost.

Government of Puerto Rico  
OFFICE OF THE COMMISSIONER OF INSURANCE

**WARNING TO THE CONDOMINIUM ASSOCIATION REGARDING THE  
PROVISIONS OF THE INSURANCE CODE REGARDING CERTAIN  
DEDUCTIBLE OPTIONS IN PROPERTY INSURANCE FOR  
CONDOMINIUMS**

Public Law No. 273 of August 18, 1999, from hereon, "the Law," was approved with the purpose of adding Article 27.081 to the Insurance Code of Puerto Rico, with the purpose of, among other things, requiring that insurers who process property insurance in Puerto Rico offer as option a clause indicating a deductible prorated in percentage terms in all the policies that cover or shall cover condominiums for windstorm or earthquake hazards. For these purposes, the Law establishes the following:

*"Unless the insured or the prospective insured person chooses another arrangement, each insurer shall offer as option a clause indicating a deductible prorated in percentage terms in any property policy that covers or shall cover a condominium for windstorm or earthquake hazards. Said deductible prorated in percentage terms shall require the application of deductibles in the case of losses in units of a condominium or in its common areas, in proportion to the ratio between the area of said units and the common areas thus affected and the total area of the condominium."*

This means, among other things, that if this alternative were chosen, only a part of the deductible that would apply to the entire condominium would be applicable to each apartment affected by one of the aforementioned hazards. That is to say, if the horizontal surface of an apartment were, for example, 2% of the total horizontal surface of the condominium, and the condominium had a global deductible of say \$100,000, the deductible that would be applicable to said apartment would be \$2,000, or 2% of \$100,000. A similar process would be applicable in the case of common elements insured under the policy.

You should consult with your agent or your insurance broker who should offer you a detailed explanation of this matter.

If you should have any questions regarding the aforementioned Law and its application, you may contact the Office of the Commissioner of Insurance at 722-8686 ext. 2243.

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### Coverage Exemption for Unit Owners

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It is hereby agreed and understood that the scope of the coverage provided under the section titled Articles of Building Unit Owners of Endorsement DP 17 66 07 88, Coverage for Unit Owners, is as follows:

This policy covers the interest of the insured in all common elements and general common elements of the condominium<sup>11</sup> against all direct damages caused by one or more of the insured risks. In the case of loss, this insurance will be excess over the amount that is recovered by the property insured herein under the master policy in the name of the corporation or association of owners.

Likewise, it is hereby clarified that the Coinsurance Clause does not apply to the property for which this endorsement is extended either, since the applicable Loss Adjustment Clause is that which appears under Endorsement DP 17 66 07 88, Coverage for Unit Owners.

The remainder of the provisions of this policy are applicable.

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<sup>11</sup> As defined in the Horizontal Property Act, Public Law No. 104 of June 25, 1958, as amended.

**Extension of Coverage A  
Unit Owner Form**

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It is hereby agreed and understood that the scope of the coverage provided under Coverage A, Housing, is as follows:

This policy covers the interest of the insured in all common elements and general common elements of the condominium<sup>12</sup> against all direct damages caused by one or more of the insured hazards. In the case of loss, this insurance will be excess over the amount that is recovered by the property insured herein under the master policy in the name of the corporation or association of owners.

Likewise, it is hereby clarified that the Coinsurance Clause does not apply to the property for which this endorsement is extended either, since the applicable Loss Adjustment Clause is that which appears under policy form HO 00 06 04 91, to which this endorsement is attached.

The rest of the provisions of this policy are applicable.

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<sup>12</sup> As defined in the Horizontal Property Act, Public Law No. 104 of June 25, 1958, as amended.