"ANOTHER PREMIUM INCREASE? WE CAN'T AFFORD IT!"

MACKOUL® RISK SOLUTIONS INSURANCE

Explaining Premium Increases

By now, I'm sure we are all tired of the hard market. Every single association has seen increases each of the past few years.

The question is, how much of an increase?

Explaining Premium Increases

An association with an insurance company that specializes in co-op and condominium insurance may have "only" seen increases of 15-20% each of the last few years.

Most associations have enough funds in their reserve to cover those kinds of increases, but what about the association that has had their insurance coverage canceled because they have an unfavorable loss history? Or because their electric contains Federal Pacific Stablok circuit breakers, which are frowned upon in the insurance industry?

We have seen scenarios in which these associations had their insurance premiums skyrocket. One property we know of increased from $200,000 to almost $900,000 because they have an unfavorable loss history and, to make matters worse, ongoing work on the building!

We have seen plenty of other associations that have faced 100%, 200%, or higher increases. In some instances, these increases could last for several years until the loss history becomes more favorable, upgrades are done to the building, or the market changes and carriers decide they are going to look the other way.

Why Premiums Have Been Increasing the Past Few Years

Property Policies

- Inflation
- Increased Cost of Construction Materials
- Increase in Catastrophic Storm Size & Frequency

General Liability Policies

- Social Inflation
- Increased Frequency and Severity Regarding Labor Law Claims (New York)

Umbrella Liability Policies

- Carriers No Longer Writing
- Carriers Becoming More Selective
    - Building Updates
    - HPD & DOB Building Violations in 5 Boroughs of NYC

Reinsurance

Where does the money to pay the increased or unbudgeted insurance premiums come from?

Since it is a common expense, if there is enough money in the reserve account, it would come from there.

What if the association doesn't have enough in the reserve account or doesn't want to exhaust it?

Options:

1) Finance the insurance premiums.
2) Take a loan. For a co-op, they can refinance the mortgage and a condominium can take a loan.
3) Raise Maintenance Fees.
4) Assess the Owners.

Where does the money to pay the increased or unbudgeted insurance premiums come from?

Finance the Insurance Policies

Many insureds finance their insurance policies each year because the insurance company does not allow installments and they either don't have the money to pay the entire premium in advance or they don't want to. Financing allows premiums to be paid in multiple installments.

After the insured pays the initial deposit, usually a minimum of 25% of the premium, the finance company pays the insurance companies and the insured repays the finance company in installments, usually as low as 3 and as many as 10, while paying interest to the finance company. The loan is generally one year, as that is typically the policy term. This option can work if either the association has enough funds to pay the deposit and installments, will have enough to pay each installment once they collect the monthly maintenance or can collect enough money to pay the monthly installments.

Where does the money to pay the increased or unbudgeted insurance premiums come from?

Take a Loan

Refinancing a mortgage or taking a loan are not quick and easy options. Not really feasible in this instance, especially considering it is unknown how long the increased premiums will last.

Raise Maintenance Fees

Raising maintenance fees may work in some situations if the shortfall isn’t too large and the association has the funds available to pay the insurance policy in full or is able to finance the insurance policies. Sometimes, the increase is so drastic that the association doesn’t have enough available to even pay the deposit on the finance agreement or the minimum earned premium (MEP) some policies contain. In addition, many boards don't want to raise maintenance, as once the figure goes up, it rarely comes back down.

Where does the money to pay the increased or unbudgeted insurance premiums come from?

Assess the Owners

In some instances, an assessment may be the only way to go. When you divide the increase in insurance premiums by the number of units, it is a much more palatable figure.

We had one association that had an increase of about $130,000, and their initial response was, **“We can't afford it.”**

When I told them to divide that figure by the number of units (671), it worked out to $193 per unit. Nobody wants to pay an assessment but looking at it on a per-unit basis ($193) vs. the overall amount ($130,000) is much easier.

As with raising maintenance, I know plenty of boards don’t like to assess owners, but the truth is that one or the other, or both, are a necessity sometimes.

Over the course of time, expenses are going to increase. That is simply a part of life. If the amount of money the association is taking in doesn’t increase each year, or at least occasionally, how can you expect to pay your expenses? It’s like an individual who never gets a salary increase, yet their expenses increase each year. At some point, there is going to be the need for rainy-day funds. ***Some insurance company executives are wondering if the hard market is going to be the new norm, so better to be prepared***.

Property Deductible

Something that can be done in conjunction with any of the options above is to increase the association's property deductible.

Not only does this reduce the association's insurance premium, it restricts the ability to put in smaller claims, which are what normally gets an association in trouble, but having a higher deductible also allows the board to assess the owners each time there is a claim (assuming there is a claim) a proportionate amount of the property deductible.

Owners can submit the assessment to their insurance carrier for reimbursement.

In New Jersey, owners of a condominium are typically responsible for the association's deductible if their unit is affected.

What is Loss Assessment?

If the owner has Homeowner's Insurance, their policy should include a coverage called Loss Assessment.

Loss Assessment provides coverage for an assessment that results from a covered peril under the homeowner's policy, like a fire, burst pipe, or a hurricane, where the association either does not maintain adequate coverage or to make up for the deductible.

Most homeowner's policies cap the amount they will reimburse towards a deductible, but even if that cap is $1,000, an association with 50 units and a $25,000 deductible would only have a $500 assessment. An association with 100 units would only have a $250 assessment. Loss Assessment is a very affordable coverage, so each owner should make sure they have at least $10,000, which is generally about $4.

Who’s Responsible for the Deductible?

Typically, in a cooperative or condominium building, the association is responsible for their deductible if a claim has been reported to the association's policy. It does not matter if damage has been done to the common area or to someone's unit of which certain portions may be the association's responsibility. The association's deductible is the association's responsibility.

In New Jersey, the New Jersey Condominium Act basically puts the onus of the association's deductible on any affected owners. So, for example, if a fire damaged four units and the association had a $10,000 deductible, the affected owners would all be responsible for $2,500 each of the association's deductible. The association is typically only responsible for the deductible or a portion of the deductible if the common area is affected. Many associations are implementing a deductible resolution to the bylaws to clarify the responsibility of the deductible and, in some instances, amend it further.

In the event an owner is responsible for the association's deductible or a portion of it, their homeowner's policy should pick it up.

Homeowner's Insurance

Something like this is one of the many reasons boards should require that owners have Homeowner's Insurance. If it's not required in the governing documents, a conversation with corporate counsel about what options are available should be had.

Knowing all owners have insurance provides the board not only with options in terms of assessing owners but all owners having insurance helps keep the peace when a claim occurs.

If an owner experiences damage to their unit or contents and they have no insurance, they are more apt to sue another owner or the board. If an owner has no insurance and their apartment becomes uninhabitable due to a covered peril like fire, and they don't have the ability to rely on an insurance policy to pay their additional living expenses, they are more apt to sue another party.

Overall, each owner having insurance can help keep the association's loss ratio down in some instances. Lower loss ratio = lower insurance premiums.

How Do We Monitor Homeowners Insurance?

If Homeowner's Insurance is required by the governing documents, *it must be monitored to ensure compliance.* What's the best way to do this?

1) Hopefully, the insurance requirement includes what coverages are required to be maintained and minimum limits. If not, some owners may have insurance coverage, but not the coverages the board would want, and their limits may be insufficient.
2) Each owner should be required to submit proof of coverage initially that meets the requirements.
3) Upon expiration of each owner's insurance policy, they should be required to submit proof that their insurance coverage was renewed. You can't just require proof once a year on one common effective date, as each owner is going to have a different expiration date. If you have 60 owners, that means an average of 5 owners a month will be expiring. If you only request proof once a year, say January 1st, and an owner has an expiration date of January 15th, their policy may expire and not be renewed two weeks later.
4) Find a company to do it for you! The Board and Property Manager are not equipped, nor do they have the time to handle this. We provide this service, and I am sure other companies do too.

In this day and age, and with this crazy insurance market we are in, every building needs to be prepared to have funds available in the event it is needed. We are here to help in any way we can.

Thank you for attending!

Contact Information:

Edward J. Mackoul, CPCU, CIC

ejmackoul@mackoul.com

(516) 279-1233

Eric Eggert, CIC, CIRMS

eeggert@mackoul.com

(516) 279-1239

www.mackoul.com

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