ADJUSTING TODAY

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EDITOR'S NOTE

For millions around the world, apartment or condominium living brings a dimension of simplicity and freedom to their lives not typically found in traditional home ownership. Maintenance issues, and the desire and ability to enjoy flexible, mobile lifestyles—including having a dwelling in more than one location—continue to make apartment and condo living more popular than ever.

But while simplicity may be one of the benefits of this lifestyle, another aspect that must not be oversimplified is the insurance program that protects the parties and properties involved. In fact, given the myriad conditions, relationships and exposures that can exist with multi-family complexes, making sure the right insurance program is in place merits even more foresight and planning than arranging a conventional homeowners policy.

In this issue of Adjusting Today, *insurance expert Paul O. Dudey takes an in-depth look at this important but often inadequately addressed subject, including the insurance risks and needs that should be considered by those who own, manage or reside in cooperative or rental apartments, or condominiums. He discusses the differences between the three, the various risks to which they are exposed, and the coverages available to protect them.*

In addition to Mr. Dudey's article, veteran public adjuster Scott Davidson draws on his extensive background to offer a companion piece focusing more closely on one of the most difficult types of losses to detect and settle, but one to which many multi-family complexes are exposed—hail storm damage. This is important and informative reading for anyone with an interest in these types of properties.

—Sheila E. Salvatore, Editor

Multi-Family Complexes: (Apartment and Condo)

An In-Depth Look at Insuring the Many Exposures and Losses

By Paul O. Dudey, CPCU

There are three common types of apartment complexes: rental apartments, condominiums and cooperative apartments. As to risk and insurance matters, all three have many characteristics in common, but there are also important individual differences in the precise details of ownership, owner's and resident's ownership interest and legal rights and responsibilities, and the way they are insured for property loss, legal liability, and other loss exposures. This article will describe several of these important differences, and will discuss in considerable depth how the three types of apartment complexes should be insured, as well as what kinds of losses may be encountered. We will also offer some helpful advice on loss prevention or control.

Rental Apartments

These are defined as multi-resident buildings owned by an individual, partnership or corporation, with

all or most of the apartment units rented to others. The rental usually involves a lease of the premises, spelling out the conditions, privileges, and responsibilities of the owner and the residents.

Condominiums

Condominiums are a relatively new form of apartment ownership, having been created by the passage of condominium laws in various states in the 1960s and having gained prominence as a preferred type of apartment ownership in the 1970s and 1980s. Two kinds of ownership are involved—individual unit owners hold title to the space in which they live, and unit owners in common—usually as compulsory members of a condominium association—own the common property, often including the entire shell of the apartments with the individual unit owner owning only the interior of the unit up to the interior of the exterior "bare walls," usually including the floor and ceiling as well.

The details of ownership, privileges and responsibilities of the unit owner and the association of unit owners are described in a document in most states called the condominium declarations, or in a companion document—the condominium bylaws. The unit owners have the right to rent out or sell their units to someone else, although the association may in some cases screen the rental or sale and hold the right of first refusal if the prospective renter or buyer does not meet their standard of ownership.

Cooperative Apartment

This type of common ownership of apartments predates condominium ownership by many years, and was and still is found principally in large urban areas such as New York City and Chicago. The individual residents of the "co-op" hold life tenancy to their apartments and own stock in the corporation that owns the property, usually in the same proportion to the total value of the project that their unit's value or area bears in relationship to the total value or area of the complex. Management of the property is usually handled by a management firm hired by the co-op owners or by an association elected by the owners. As with condominiums, the individual owners may lease out or sell their unit, but in some cases only with approval of the association.

Insurable Property Exposures

Each of these three types of apartments have many insurable property exposures, but with some important differences that must be considered in arranging insurance. All call for building management to purchase insurance on the resident occupied buildings as well as any other property such as a clubhouse, swimming pool, health facility, tennis court, golf course and related personal property, etc., that may require insurance.

Personal property owned by residents is usually the responsibility of the residents to insure, but there may also be personal property owned by the apartment building owners—and this should be included with the building insurance. Standard building coverages (such as provided by the Insurance Services Office [ISO]) will include a description of personal property items that may be included

as building at the usually lower building insurance rate. Other personal property not so listed must be covered, either specifically or under blanket coverage with the buildings, using the personal property insurance rate.

Generally, insurance with at least an 80 percent coinsurance clause (unless replaced by an agreed value clause) is required, or if multiple buildings are involved, blanket insurance for 90 percent of current value is suggested. Also recommended—especially with buildings more than one or two years old—is replacement cost coverage, which covers the cost of replacing new for old, with no deduction for depreciation as would be the case with actual cash value (ACV) coverage.

Additional Coverages–Coverage Extensions

In addition to the basic buildings and personal property coverages, most forms also provide a number of additional coverages and coverage extensions. Below is a summary of these as provided by the ISO form: (Refer to the form itself for various limitations and exclusions found in these sections.)

4a) Debris removal, pays up to 25 percent of the amount of the loss (not exceeding the limit of insurance for the combined loss) plus $10,000 (can be increased);
4b) Preservation of property removed to protect it from loss or threatened loss for up to 30 days;
4c) Fire department services charges, up to $1,000 with no deductible;
4d) Pollutant clean-up and removal, up to $10,000 (can be increased);
5a) Newly acquired or constructed property, for 30 days or until policy expires if earlier, $250,000 buildings, $100,000 business personal property;
5b) Personal effects and property of others, up to $2,500;
5c) Cost of research, valuable papers and records, up to $2,500 (can be increased);
5d) Property off premises (except in or on a vehicle, in custody of insured's salespeople, or at a fair or exhibition), up to $10,000;
5e) Outdoor property, as listed, against limited listed causes of loss for no more than $1,000 ($250 per tree, shrub, or plant) per occurrence.

Each of items 5a through 5e is additional insurance with no coinsurance applying, but applies only when 80 percent or higher coinsurance or equivalent is used on the basic property insurance.

Covered Causes of Loss

Three levels of choice of covered causes of loss (formerly referred to as "perils insured against") are generally available, although there are considerable variations in the details of coverage from one insurer to another. Care should be taken to compare the list of covered and excluded or unmentioned causes of loss when comparing coverage choices.

Basic coverage includes only a limited group of covered causes of loss—fire, lightning, wind and hail (excluded in some hurricane-prone areas), explosion, damage by aircraft or vehicles, and riot or civil commotion, and usually vandalism or malicious damage, along with sprinkler leakage for buildings with automatic sprinklers, sinkhole collapse (but not mine subsidence), and volcanic action. Although the least expensive form, this form should be avoided as there are too many other perils not covered here that can also produce severe loss. Its most common use is as a means for underwriters to provide minimal coverage for substandard properties.

Broad Form coverage expands the list of causes of loss to include falling objects, weight of snow, ice or sleet, and water damage (but not flood or overflow of natural bodies of water, or sewer backup) and, as "additional coverages," glass breakage and a limited form of collapse.

Special Form coverage applies to any risk of direct physical loss not

otherwise excluded or limited. While theoretically the broadest coverage available and the most expensive, this form can be a trap for the unwary. There are a number of versions of this form with substantial variation in the wording of the exclusions—some of them even taking away coverage that would be provided under the Broad Form.

This is particularly true following the addition of the "concurrent causation" language several years ago, which excludes loss by any excluded cause "regardless of any other cause or event that contributes *concurrently or in any sequence to the loss*." Interpretation of this language is still up in the air, as in some cases it seems to work an undue hardship on insureds. While all three Causes of Loss forms have this language, losses involving a named cause and an exclusion seem more likely to be resolved in favor of coverage for the insured than under the Special Form, which does not specifically name individual causes of loss, except for a list of "specified causes of loss."

If you are considering use of the Special Form, be sure to make a line-by-line comparison of the Special Form exclusions with the coverage offered under the Broad Form. Excluded from all three Covered Causes of Loss forms are each of the following which, to be covered, require separate insurance:

1) ***Equipment Breakdown***
   Insurable under equipment breakdown forms, which can be covered separately or included under the package policy as a separate item of coverage.
2) ***Earthquake***
   (as opposed to "volcanic action" which is covered)
   Insurable under separate earthquake insurance. A brief discussion of this important and rather complex coverage is included later in this article.

3) ***Flood***
   Coverage is available only through a separate federally sponsored flood insurance program or by a few specialty underwriters, mainly in the surplus lines markets.
4) ***Wind and Hail***
   As noted earlier in this article, in a few hurricane-prone areas along the Atlantic and Gulf coasts, underwriters have imposed a mandatory wind and hail exclusion under the property insurance and instead, offer separate wind and hail coverage through a joint underwriting pool.
5) ***Ordinance or Law***
   (loss or increased cost due to enforcement of any ordinance or law involving repair or construction)
   This important topic is also discussed later in this article.
6) ***Motor Vehicles (other than vehicles not licensed for highway use), Aircraft and Marine Property Exposures***
   These are also excluded and are the subject of separate forms of coverage. For motor vehicles, if a broad enough spread of risk exists (unlikely for most apartment risks) and the loss experience has been satisfactory, self-assumption of all but perhaps the most expensive vehicles or a high deductible overall can be considered.
7) ***Accounts Receivable and Records and Valuable Papers***
   Only limited coverage (usually insufficient for the insured's needs) is provided for these types of losses. Again, separate insurance is available here.
8) ***Crime***
   Burglary, robbery and theft, as well as employee dishonesty

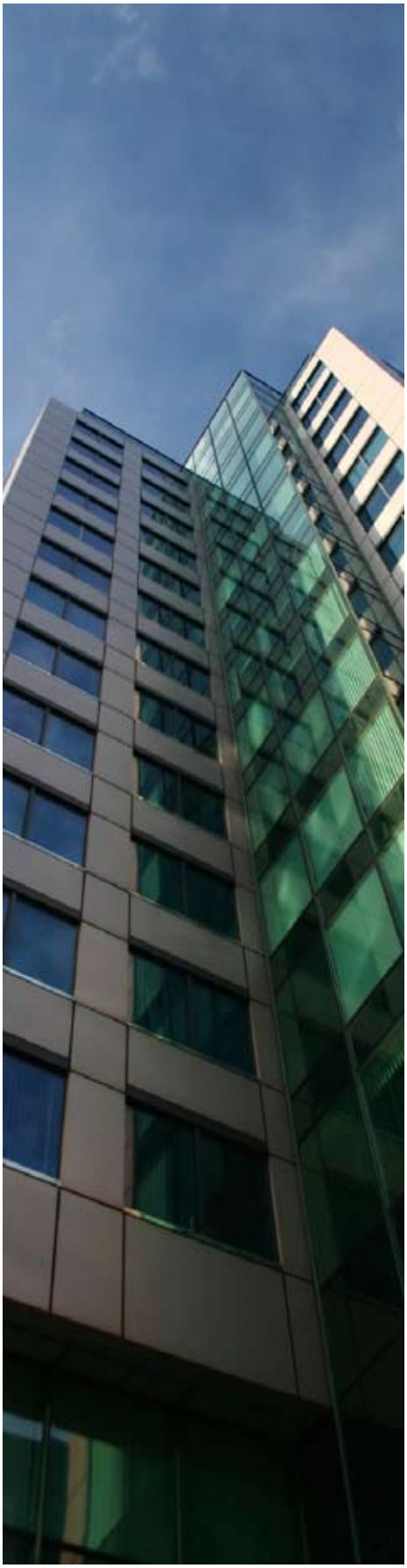
require separate coverage, although limited coverage is sometimes offered.

Also excluded from Covered Causes of Loss forms, but generally not insurable, are loss by wear and tear, gradual deterioration, rust, corrosion, latent defect, insect or animal damage, etc. The question is still open as to what, if any, effect the "concurrent causation" exclusionary language has on losses in these categories when damage due to any of these produces other not-excluded damage. Previously, only the excluded damage, i.e., the rust damage requiring repair, would not be covered—but resulting damage to other property would be covered. In considering what coverage to purchase, comparison of exclusions from form to form is most important.

Deductibles

Most insurers insist on a mandatory deductible clause applying per occurrence to all or most of the insured causes of loss. A $100 or $500 minimum deductible is common, but higher optional deductibles at progressively reduced premiums are generally also available. In deciding what level of deductible to choose, several factors should be considered:

A) Available premium savings in dollars compared with the insured's probable increased participation in any future loss payments.
B) Past loss history—the frequency and severity of past losses as a measure of the savings or increased cost with various deductible levels. Keep in mind here that underwriters tend to become disenchanted with payment of frequent claims, irrespective of their size, so for an account that tends to generate frequent small losses, rather than attempt to collect on all of them from the insurer, an insured might be well-advised to select a higher deductible at a reduced premium and instead absorb these small losses.
C) Spread of risk—where there is a large enough spread of risk to give some credibility to past loss experience and high enough premium overall to offer sufficient premium savings with a higher deductible, an intelligent choice of what deductible level to purchase can be made. If this analysis is accompanied by a well-designed safety and loss control program (discussed later in this article) so that frequency and severity of



losses are reduced, the higher deductible will very likely be more beneficial. Where spread of risk is lacking, the same opportunity for savings does not exist, and choosing a higher deductible becomes more of a gamble.

Special Condominium Insurance Problems

For condominiums, a further problem must be considered: How much of the building must be insured by the condominium association and how much of each unit by the unit owner? Here it is necessary to look to the condominium declarations and bylaws to see who is to insure what. Under the "bare walls" provision referred to earlier, the unit owner covers the interior of the unit up to the bare floor, ceiling (or roof) and exterior walls of the unit and the association insures the remainder of the building. Interior paint, wallpaper, floor coverings, or other interior decor is the unit owner's responsibility, and should be covered under the unit owner's condominium policy along with the unit owner's personal property.

The "bare walls" concept was most widely used during the early days of condominium development, but now has largely been superseded by a provision calling for the association to insure all property originally included in the unit, but the unit owner to insure additions made by the unit owner. This can present problems when a unit is sold to a new owner after a previous owner has made substantial improvements and additions. Where this situation applies, the new owner should clarify with the association in writing who should insure what and set up the insurance to fit.

But beyond these two, there are a wide variety of condominium declaration or bylaw provisions in this area, so in arranging the association's coverage, these must be analyzed and appropriate insurance arranged to reflect the actual value of the property to be insured by the association. And the individual unit owners should be alerted to these provisions as well so they can arrange for proper coverage under their individual condominium unit owner's policies.

Also important is the unit owner assessment feature of most condominium declarations, which can mandate that the unit owners make up for deficiency of income to the association, especially following an uninsured or only partially insured loss. Individual unit owners usually have a small amount of assessment liability coverage in their unit owner's policy ($5,000 or $10,000 is common) and can purchase higher insurance limits if desired.

A further problem with condominiums is how to proceed if, after a major loss, it is deemed for whatever reason impossible or undesirable to rebuild, or a major number of unit owners prefer to abandon the property and take their share of the insurance proceeds as cash. The condo declarations will usually provide for this, stating what proportion of the unit owners (usually a substantial majority—such as 75 percent or 80 percent) must agree to the abandonment. The same often applies to cooperatives.

Special Cooperative and Rental Insurance Problems

Cooperative apartments and rental apartments have similar insurance needs (not nearly as complex as condominiums) and with only a few differences. In both cases, the residents insure only their own personal property and personal liability, and the apartment owners insure the buildings and any personal property belonging to the apartment owners—furnishings in a clubhouse, exercise facility, etc.

The major problem in both cases is in identifying the respective responsibilities of landlord and resident in such areas as damage to the premises, repair and maintenance, and cancellation or continuation of the lease after loss.

Co-op owners also usually have the same potential as condominium unit owners for individual assessment to make up for deficient income by the association. As with unit owners, this can be covered by insurance if the assessment is due to inadequacy of a covered cause of loss.

Ordinance or Law Exposure

Municipal building and zoning ordinances, along with county, state, and federal regulations, have proliferated in recent years, creating a potentially severe exposure for apartment complexes covered only by basic property insurance.

If there have been any significant changes in building or zoning laws since the units were built that would:

a) require demolition before reconstruction; or
b) substantially increase reconstruction cost or, as was discovered frequently in the aftermath of Hurricane Andrew in Florida, if the construction was not up to code at the time it was built, then ordinance or law coverage should be added.

Three coverages are available:

1) Contingent Liability for Operation of Building Laws coverage, which covers the loss of the undamaged part of a damaged building that must be demolished due to the requirement of a building ordinance or law (the basic property coverage applies only to the portion damaged by the covered cause of loss);

2) Demolition insurance, covering the cost of demolition of undamaged portions of such a building and the cost of site clearance; and

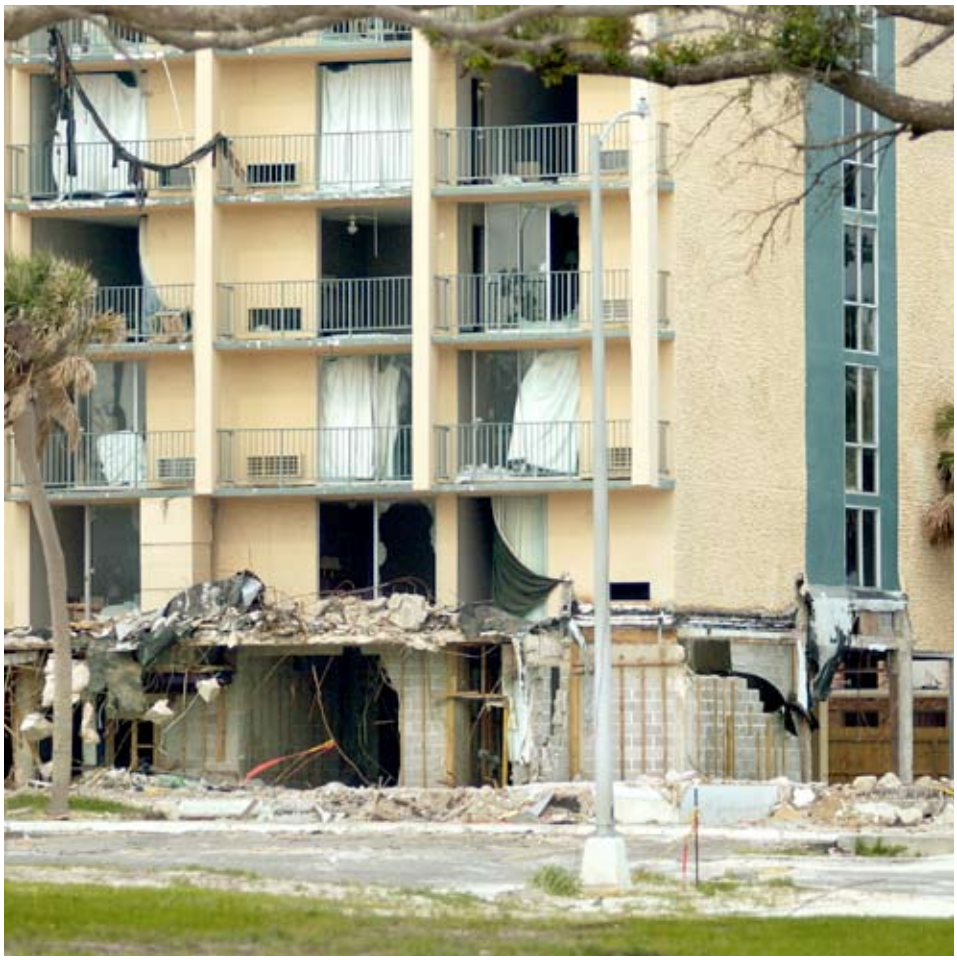
3) Increased Cost of Construction insurance, covering the additional cost of rebuilding to comply with current law. An example of the impact that application of building or zoning laws can have is a claim for a condominium loss arising out of Hurricane Andrew. Fortunately the condominium

association had purchased ordinance or law coverage as a part of their property insurance program.

The insurance company adjuster's initial estimate of $825,000 quickly was revised upward to $10.5 million. Moreover, there was another $6.5 million for increased cost of construction due to ordinance or law requirements. Items covered under the ordinance or law provisions included the cost of such things as:

- Fire stops between units, originally designed with a suspended ceiling system to serve as an open return air plenum;
- Exterior curtain wall not secured up to current code;
- Black iron used instead of more fire-resistive materials;
- Removal of asbestos insulation in the suspended ceiling cavity;
- High-wind-load windows able to sustain the impact of a two-by-four board moving at 35 mph and only break like auto windshield safety glass;
- Balconies had 8-inch spacing between railing balusters instead of the 6-inch maximum spacing required by code;
- Fire sprinkler system with complete plumbing and head installation to each town home and common areas was required;
- Elevators had to be brought up to current code; and
- Emergency generator had to be moved from first to second floor to avoid exposure to flood damage.

How do you know whether ordinance or law coverage is needed? In most jurisdictions



and with most building or zoning laws, existing properties are "grandfathered" when the law changes and property owners need not comply until such time as new building permits are required, when major changes in construction are planned, or when the property is significantly damaged as by fire, wind, explosion, flood, earthquake or the like.

There are exceptions—where changes require immediate compliance, but these are rare and are usually accompanied by sufficient publicity to alert owners to the need to comply.

Persons charged with the risk management function should consult with the government officials in charge of enforcing the building or zoning laws to determine what changes in construction methods or materials would be required following a loss and what degree of damage (frequently 50 percent or 75 percent) would call for demolition of existing property in order to rebuild. Also, the question of whether the property would be rebuilt—on the same or perhaps on another site—should be addressed and taken into account in arranging the insurance.

When answers to these questions have been found, the risk manager can then proceed to arrange adequate ordinance or law coverage. (For an in-depth study of this coverage, refer to *Adjusting Today* Ordinance or Law edition.)

Lease/Declaration Provisions

Most important in arranging insurance for apartments or condominiums is a study of the pertinent provisions of the leases or condominium declarations being used.

Lease Cancellation Clause For rental apartments other than cooperatives, a major provision is the lease cancellation clause. It will tell under what circumstances the lease may or must be cancelled by the owner or the resident. Particularly important is the provision relating to inability to occupy the premises following damage by fire, wind or other loss. These provisions vary widely from lease to lease, and with each variation a different approach to insurance needs may be required.

In one typical provision, rent continues for a stated time (60 days is common) after which, if the premises have not been repaired sufficiently for reoccupancy, the lease may be cancelled at the option of the resident or the landlord, or in some cases by either one. Alternatively, the lease may allow immediate termination of rent if the premises clearly cannot be restored to occupancy within the stated period of time. The effect of the cancellation-by-loss provision (assume a 60-day clause) may be to cost the resident two months rent (recoverable under the resident's policy Item D, additional living expense coverage) after which time, the resident having moved elsewhere, the lease can be cancelled. If the owners intend to repair or rebuild but cannot do so within the 60 days, they can negotiate with the present resident to resume occupancy at the same or perhaps higher rent, or can find new residents.

For the landlord, the loss of rents can be covered by rental value insurance, a form of business income coverage which can be added to the property or package insurance program. If the property is not rebuilt, the rental value coverage would still apply, covering the rental loss for the time it would have taken to rebuild.

Another provision sometimes used in leases is a rental abatement clause which, instead of allowing cancellation of the lease, permits abatement of the rent until the premises are again habitable. This has the advantage for the resident of preventing the landlord's cancellation of a lease favorable to the resident and gives a further incentive (along with a similar requirement of the rental value insurance) to the landlord to proceed quickly on repairs in order to begin collecting rent again as soon as possible.

Insurance Provisions

Both the condominium declarations and the apartment leases will generally contain an insurance clause spelling out who—condominium unit owner or unit owners in common (or the association); co-op resident or residents in common (or association); or resident or owners—will carry what kinds of insurance and generally for what minimum amounts.

These provisions can vary widely and should be clarified for anyone charged with responsibility for arranging the insurance. Also, their sufficiency or lack thereof should be analyzed and recommendations made to correct any deficiencies in amounts or limits of coverage or omissions of any important coverages. It is relatively simple to bring the actual insurance up to the requirements spelled out in the condo declarations or lease. But where the stated requirements are inadequate, making changes can be a major undertaking. Also, the purchase of insurance not required by the declarations or lease can give rise to criticism by some condominium or co-op occupants and possibly even suit against the managers, officers or board for allegedly wasting assets intended for other purposes.

Conflict Over Coverage Interpretations

Insurance language is general in nature and often quite vague as to its intended application to a particular set of circumstances. It should be kept in mind that in the absence of clear evidence of the intent of the parties in negotiation of the details of coverage, an ambiguity may be found to exist. In most cases involving insurance on apartments, the insurance policies are drafted by the insurers or their representatives and

simply offered to the insured with little room for modification. This being so, the general rule is that the benefit of any reasonable interpretation of the intent of the coverage lies with the insured.

Repair and Maintenance Provisions

Apartment leases will usually have a repair and maintenance provision which, depending on the exact wording, can prove troublesome for the resident. While intended to spell out who—landlord or resident—is responsible for routine repairs and maintenance, painting, minor plumbing repairs, etc., the language is often so broad that it also appears to transfer to the resident the responsibility for repairs following a major loss. This is especially possible if the insurance clause isn't clearly drawn and sometimes even appears to allow the owner to pocket the insurance money while requiring the resident to pay for the repairs.

In drawing up new leases or condo declarations or, given the opportunity, modifying existing ones, care should be taken especially with the insurance and repair and maintenance clauses.

Liability Exposures

Significant liability exposures also present a number of problems that apartment managers and residents must address:

1) How much is enough liability insurance? This is one of the most difficult questions to answer. The larger the apartment complex and the closer to other major properties, or the more children present, the greater the liability exposure. In today's climate of mega-million dollar liability judgments, high liability insurance limits are clearly needed. The problem is made worse by the fact that once the liability limits are exhausted, claim can still be made against the remaining assets.

A common practice is the purchase of several layers of liability insurance; a primary layer above whatever deductible seems feasible, a $1 million to $5 million umbrella layer above that—perhaps broader than the general liability coverage—and, if affordable, one or more

layers of excess coverage of $1 million or more over that.

Generally included in the umbrella layers are such added coverages as automobile liability and professional liability. Some umbrella policies provide almost the equivalent of "all risk" liability insurance, being excess over any primary liability insurance with a "drop-down" coverage over a large uninsured deductible for liability exposures not covered by primary insurance.

2) Coverage beyond the commercial general liability (CGL) policy will often also be needed. Among the liability exposures likely to be found by apartment owners but excluded from the CGL are:
   a) ownership or use of automobiles;
   b) professional liability;
   c) pollution liability;
   d) liquor liability;
   e) directors and officers liability insurance;
   f) workers compensation and employers liability.

2a) If motor vehicles are owned, leased, or rented by the apartment owners, or used by the owners or their employees or by residents or unit owners on apartment business, auto liability insurance is needed.

Even if there are no owned or leased vehicles, non-ownership coverage should be obtained covering the apartment owner's liability when employees, residents or unit owners, or others operate motor vehicles on behalf of the apartment owners. Note that motor vehicles not used off premises and not licensed for highway use (lawn mowers, golf carts, etc.) are exempt, as their use is generally covered under the CGL insurance.

Substantial limits of automobile liability should be purchased as well. If umbrella coverage is used and includes the auto liability, the umbrella underwriters may well set mandatory minimum primary auto liability limits which must be carried to avoid a gap in coverage.

2b) Professional liability exposures may be encountered if anyone associated with the apartments is engaged in professional activities—law, architecture, etc.—on behalf of the owners. Separate professional liability insurance is needed for this exposure, preferably naming both the professional persons individually and the apartment owners.

2c) Pollution liability as a major exposure is relatively new, being in large part a creature created by government pollution laws. This is a complex subject, too involved for adequate treatment here. It is sufficient to say here that if any pollution exposure is even remotely suspected, call in experts in pollution insurance, pollution control and legal interpretations.

2d) Liquor liability—If liquor is served, as at apartment sponsored parties, picnics, or the like, separate liquor liability insurance should be provided.

2e) Directors and officers liability —Condominium and cooperative apartment directors and officers can be sued by residents, unit owners

or outsiders for various alleged offenses. Many of these offenses are outside the CGL coverage but can be covered by separate directors and officers liability insurance. Also, the contract with the directors and officers may allow the owners or association to be joined in the suit or may require them to provide this insurance on behalf of the directors or officers.

2f) Workers compensation and employers liability—If the apartment complex has employees, workers compensation insurance may be required, depending on the number of employees and the workers compensation laws of the state where the apartments are located. Even when workers compensation insurance is not required, employers liability insurance may be in order as employee injury is excluded from the CGL.

A possible pitfall here is the use of contract labor rather than employees. In certain circumstances, they may fall within the meaning of "employee" to bring the employee exclusion of the CGL into effect. Unless at least employers liability insurance is carried, an uninsured catastrophic loss could result.

3) Care, custody, and control—A major problem for residents or unit owners, probably in most cases less so for owners and landlords, is the care, custody and control exclusion of the CGL and the residents' or unit owners' policies. This excludes coverage for damage to property in the care, custody or control of the insured (except loss involving fire, smoke or explosion). If the apartment owners allow residents to use a common area for storage, this exclusion could also be a problem for the apartment owners.

Coverage for this exposure is somewhat expensive; an alternative solution could be a reciprocal waiver of subrogation agreement between owners and residents, so the resident or unit owner's insurer, having paid their insured for the loss, cannot sue ("subrogate" against) the apartment owners for their negligence or vice versa.

4) Among other CGL exclusions are expected or intended injury and war risks, neither of which is generally insurable (with some notable exceptions: marine war risks may be covered under some marine forms and personal injury coverage of the CGL will pick up some liability exposures such as libel, slander, malicious prosecution, etc.) that fall outside of bodily injury or property damage liability and might be construed as "expected or intended."

Criminal Exposures

Two major crime exposures face apartment owners:

1) Burglary, robbery, or theft by outsiders; and
2) Dishonesty and embezzlement by officers, board members and employees.

As noted earlier in this article, some crime coverage as to outsiders is sometimes offered under the basic property insurance, but dishonesty and embezzlement by insiders requires separate coverage.

Loss Control and Safety Measures

A major opportunity for dollar savings for apartment complexes, as well as optimizing residents' safety, lies in attention to loss control and safety measures—the larger the premium outlay, the greater the chance for premium savings; and the greater the number of residents, the more important the adequate safety precautions.

A great opportunity for premium savings exists in new apartment construction which, if ignored initially, may be very costly to correct later. Even if not incorporated in the original construction, savings may still be realized later for many of these items.

Take advantage of the advice offered by fire protection engineers and safety personnel to obtain minimum fire insurance rates commensurate with building construction considerations, and the lowest possible liability and workers compensation costs. Most large brokerage houses and even many smaller agencies offer these services, often at modest cost or even free to their clients.

Consider such features as:

a) Adequate exits designed for simple, quick egress but secure against unauthorized entry.

b) Smoke and carbon monoxide detectors in appropriate locations—in hallways, stairwells, garage areas and the apartments themselves.

c) Automatic sprinklers—Installing automatic sprinklers throughout, including in the apartments, may be impractical, but their use may be desirable in hallways, stairwells, meeting rooms and lounges.

d) UL-labeled fire extinguishers suitable for fighting all types of fires should be installed in the appropriate places and numbers to receive fire insurance rate credit. Residents should be instructed in their proper use. Standpipe and hose strategically placed may also be useful and may also produce insurance premium savings.

e) Fire-resistive construction (masonry walls and concrete or, less desirable, metal roof) though more costly initially, will pay for itself in premium savings over the years. Lacking that, an older frame or masonry wood-joist roof structure can be made safer by installing fire stops in the attic between the units to prevent lateral spread of fire, which can quickly involve the entire building in a fire starting in one of the units.

f) Swimming pools can be a source of multiple problems. They should be adequately fenced with gates that lock to

prevent easy access for toddlers. Pool rules should be prominently posted and enforced. The rules should be reasonable to discourage users from flouting or ignoring them, but should make clear that certain practices are hazardous and at user's risk. Lifeguards may be called for and their hours clearly posted. Adequate pool maintenance should be provided to avoid exposure to possible disease or contamination.

g) As liability (and workers compensation, though probably not a significant factor for this coverage for most apartments) insurance premiums get larger, opportunities for premium savings increase as well. But unlike property insurance which is schedule-rated, these coverages are experience-rated, with debits or credits offered from the "manual" rates for each business category based on the losses paid measured against premiums earned over the previous rating period (usually either three or five years prior to the last year). So the best way to control this cost is through vigorous safety practices.

Attend promptly to such things as adequate lighting both inside in the hallways and stairwells and outside around parking lots and entrances; repair of deteriorated carpets, sidewalks, and driveways; installation of anti-slip materials on stairs, in lobbies, hallways, and showers or bathtubs; effective elevator, fire protection equipment and alarm maintenance; and the many other things that a competent safety engineer can recommend.

If security personnel are used, be sure that they are properly trained and supervised. Be wary of overselling the value of such services to the residents. There are numerous cases of assault, rape or robbery of residents by outsiders where the residents were able to recover from the apartment owners for failure to maintain adequate security promised by the owners. Nor are condo or co-op apartment management immune from such exposures. It has long been established in courts that unit owners or co-op residents, even though co-owners of the apartment complex, have the right to sue the owners in common and their association or management for bodily injury or property damage due to their alleged negligence.

Additional Occupancies Sometimes Encountered

Many apartment complexes, especially in central city locations, will have non-residential exposures not considered in detail above. Among them are parking garages, sometimes for residents' and visitors' use only, sometimes public garages; retail stores where housekeeping can present problems; restaurants with cooking and exhaust vent hazards; and dry cleaners with potentially hazardous or flammable materials in use. Space does not permit a detailed examination of these exposures here, but they should be taken into account and analyzed for their possible impact on the apartment ownership, whenever encountered.

Common Apartment Loss Problems

Among the many problems in loss adjustment commonly encountered in apartment losses are the following:

a) Insufficient limits of property insurance to:
   1) cover the amount of the loss; or

2) satisfy the coinsurance requirement of the policy. A common failing among insurance buyers is underestimating the current value of their property, especially its cost to replace new for old, as well as the amount of loss that might be sustained. Often the amount of insurance is tied to the current amount of the mortgage, which usually does not include any owner's equity or increase in value through inflation in construction costs, leaving the insured vulnerable to coinsurance penalty on even a moderate loss and woeful underinsurance on a major loss.

b) Failure to replace the coinsurance clause with an agreed value clause or, having adopted the agreed value clause, not keeping it up to date as required annually, allowing coinsurance again to apply.

c) Not providing ordinance or law coverage or, if included, not carrying the appropriate kinds and amount of insurance to provide full recovery in compliance with current building or zoning ordinances or laws.

d) On multiple buildings or locations, using a schedule of individual amounts per building rather than blanket coverage overall.

e) Poor choice of deductibles, either too high with insufficient premium credit or too low when attractive credit for a higher deductible is available and the insured's loss history is excellent.

f) Failure to carry, or carrying an inadequate amount of, flood or earthquake insurance where the flood or earthquake exposure exists even remotely.

g) Failure to provide time element coverage such as business income, rental value and extra-expense insurance to protect the increased cost and loss of income following a major property loss.

h) Failure to insure against off-premises utilities interruption, a secondary business income loss exposure not covered by the time element coverages in "g" above but potentially severe, especially in hurricane, tornado, forest or brush-fire, earthquake or flood-prone areas, even when no direct damage to the insured's own property is involved.

i) Inadequate or nonexistent coverage against a variety of liability exposures, especially where the exposure is remote or not readily recognized. Among these are architects or engineers professional liability, motor vehicle non-ownership or hired car coverage when there are no owned vehicles, liquor liability, insurance for loss or damage to property in the care, custody, or control of the insured, directors and officers liability coverage, and employers liability for employee injury even where workers compensation may not be required.

j) Failure to safeguard accounts receivables and other valuable records and documents and to provide adequate insurance on them. Premium savings are available when adequate safe record storage is provided.

k) Failure to guard against and provide insurance on crime exposures—both external and internal—from dishonesty of employees.

Just as the nature of multi-family complexes has evolved to meet contemporary lifestyles and living needs, so must the insurance program that protects these properties respond to the specific exposures that owners, managers and occupants of these dwellings face. Designing, implementing and maintaining such a program is an effort to be taken every bit as seriously as that which went into creating the complex in the first place. It is essential to guarding the property's value—and to optimizing and preserving the safety, security and overall quality of life that the facility offers.

Paul O. Dudey, CPCU

Hail Damage Can Create Difficult Losses

One potentially serious, yet difficult-to-detect, type of loss that can strike an apartment or condo complex is hail storm damage. Scott Davidson, a public adjuster affiliated with the Texas and Colorado offices of Adjusters International—whose extensive background in dealing with claims of this type includes working with major property management firms and REITS (real estate investment trusts) across the country—has found that on-site managers often don't even realize that their property has suffered hail damage.

As clues to that possibility he advises that following a hail storm, a determination be made as to whether trees or flowers on the property have been damaged, if cars parked in the open were dented or building windows have been broken. Equally important, the many portions of the building not commonly considered subject to damage—such as window and door screens, siding, and air conditioners—may also have suffered hail damage and should be closely inspected. Perhaps the most costly and least recognized is hail damage to roofs.

Hail damage to asphalt shingle roofs is often not immediately recognized. It may take up to two or three years after one or more hail storms for the roof to begin to leak. On a flat roof, unless the hail is quite large (baseball size or more), it is also hard to detect hail damage until much later.

There are three types of roofs commonly found in multi-family housing, each with its own hail damage problems. A built-up tar and gravel roof requires that the gravel be brushed back and a core sample be removed and sent to a building forensic lab for analysis to discover possible hail damage. It is easier to see hail damage on a modified bitumen roof, as the hail usually leaves a star shape or circles around the point of impact. Rubber roofs constructed of Ethylene Propylene Diene Monomer—or EPDM roofs as they are commonly called—are unique in the way hail affects them. Although the rubber or membrane may not have been cut, the styrofoam insulation board under the rubber may have been damaged and ponding may result.

An example of hail strike assessment.

Mr. Davidson also supplied the following hail loss example, from his experience with such claims:

A condominium association faced a compounded problem when the foam roof of the condominium was extensively damaged by hail. Under the foam roof were popcorn asbestos ceilings in each unit. While the roof was being removed, the asbestos shook loose from the ceilings into each of the units. Air monitoring equipment was immediately employed and the potential asbestos hazard was avoided. The insurer wanted the insured to simply plug the holes in the roof; but to repair this kind of damage, the roof must be scarified, the process of taking off the first inch or two of foam and reapplying it. Coverage for this damage was found under the debris removal section of the policy.

Contributing:
Scott Davidson
Adjusters International

Adjusters International

CORPORATE OFFICE
126 Business Park Drive
Utica, New York 13502
1.800.382.2468
Outside U.S. (315) 797.3035
FAX: (315) 272.2054

editor@adjustingtoday.com

PUBLISHER
Ronald A. Cuccaro, SPPA

EDITOR
Sheila E. Salvatore

WEB ADDRESSES
www.adjustersinternational.com
www.adjustingtoday.com

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