Condo Insights

#28 – The impact of current economic conditions on community and condominium associations – Part 2

What are the implications of the current economic environment for community and condominium associations? Seashore condominium associations can expect higher prices for goods & services and homeowners can expect increases in HOA maintenance fees. This multi-part column will try to explain some of the factors behind these increases.

Insurance is the single largest expense item that Associations have little to no control over, and for many Associations, insurance premiums are increasing at higher rate in recent years. Insurance premium increases are the result of several factors including: additional and more severe named storms, some insurers pulling out of coastal markets, reduced capacity in the property markets, increases in the number of claims at condos that have a high percentage of rentals and lower returns on investments for insurance companies.

According to Guy Riska, an insurance broker with association clients stretching throughout the east coast and Florida, numerous severe storms have negatively affected the property insurance market in recent years, resulting in insurers realizing a total of $250 Billion (and growing) in losses paid out from just 2016 through 2021. Many of the traditional companies serving the coastal condominium market are currently in the process of rethinking their underwriting strategies in a currently transitioning market. The market for higher risks (due to location, loss history, class of business, etc.) is currently in the process of correcting rates and is expected to continue to trend upward for at least the next 2 years. None of the companies represented by Global Risk Partners Insurance Agency have been profitable for 5 straight years, so insurers are being more selective on their risks and the rates needed to consider them. Insurers have lost so much money in the last 5 years that it has completely wiped out any profits over the prior 10 years combined. Coverage limits are being reduced on higher risk classes of business such as barrier island property coverage along with rate and deductible increases across the board.

Property insurance companies rely on valuation appraisals to determine the amount of insurance for a particular building. With inflation affecting construction materials and services including flat and shingle roofing, waterproofing materials, along with increases in oil costs petroleum-based products like asphalt are also rising in cost. Property insurers are requiring updated insurance valuation appraisals because reconstruction costs have increased significantly, therefore the value of property being insured increases. When reconstruction costs increase, the amount of property insurance coverage increases, and insurance premiums increase.

Riska further states that insurance companies are in a full blown hard market due to the following: six straight unprofitable years for insurers driven by 10 straight years of eroding rates and weakening terms and conditions (soft market) resulting in significant reduced profitability for the industry; low interest rates means that there is lower investment income for insurance companies to offset rate increases; high loss activity due to the catastrophic losses; and higher plaintiff awards being paid out with loss settlements from general liability carriers. Associations have little control over insurance coverage and premiums. Insurance expenses are often 25-33% of an association's annual budget.

Many shore Associations are required to maintain flood insurance. The recently implemented Risk Rating 2.0 changes the way FEMA prices insurance and determines a property's flood risk. According to a March 2021 FEMA Bulletin, Risk Rating 2.0 will result in increases in flood insurance premiums for 79% of New Jersey properties. These increases, capped at 18% annually until the full-risk rate is realized, are also affecting Associations during this period of high inflation. However, many insured also saw great savings as part of the new 2.0 Rating restructuring.

According to the J. Byrne Agency, private flood insurance may be a less expensive alternative to the NFIP policies, but that option comes with certain risks such as losing the gradual increase in premiums and being subject to a 30-day waiting period were the Association opt to leave the NFIP and return, so Associations should consult with their insurance agent to understand those risks prior to considering private flood.

J. Byrne Agency also stated that agents market their renewals extensively to ensure their clients are getting the best coverage and premium possible. Due to the volatile marketplace and large increases in premiums, carriers are being inundated with submissions making it very difficult to provide quotes more than 3 weeks prior to expiration.

Additional columns in this series will focus on the other factors affecting Association expenses including the current labor market and the inflationary labor wage spiral affecting employers; the good and bad for seasonal service level workers; challenges facing labor-intensive service providers; how major capital projects and reserve studies are affected by inflation; and suggestions on what Association Boards should do and what they should not do in this current economic environment.

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