Condo Insights

#42 – Condominium Association Insurance – Part 2

Insurance is the single largest expense item for many associations and one that associations have little to no control over. The second article in this series will discuss factors affecting the insurance market and the challenges faced by coastal condominiums in southern New Jersey. Associations are dealing with insurance renewals that include higher deductibles, higher premiums, more exclusions, and less coverage.

Insurance premium increases are the result of several factors. Coastal areas have experienced a greater number of severe named storms. The past few years have produced some of the most difficult property insurance markets in recent years, specifically for coastal & catastrophe exposed property.

Some insurers have pulled out of coastal markets and others have reduced capacity in the coastal property markets. Coverage limits are being reduced on higher risk classes and coastal properties are facing rate and deductible increases across the board. This has been highly driven by the large number of natural disasters, the amount of disasters in excess of $1billion in property damage, and reduced capacity in the reinsurance market. Insurance carriers are altering terms and establishing separate wind/hurricane deductibles as carriers attempt to reduce their exposure to catastrophic wind events thus reducing their catastrophe reinsurance costs. Insurance carriers, especially those insuring properties in coastal areas, rely heavily on reinsurance to retain financial stability in a catastrophic disaster event. Insurance carriers experiencing these increases in reinsurance costs pass such rate increases onto the policyholders.

Insurance carriers are paying more in claims than received in premiums in recent years and experienced the highest catastrophic losses in over 2 decades. The effects of these losses will continue to materialize as many claims take time to settle and accurately reflect on the insurer's balance sheet. To return to profitability, insurance carriers will be increasing rates and tightening underwriting requirements. The insurance industry is not expected to return to profitability for several years.

Increased construction costs are a large contributing factor to increased insurance premiums. Costs of reconstruction increased over 11% annually from 2020 through 2022, lowering to just over a 4% increase in the past year. 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. Construction cost increases mean that associations may have to increase their property policy limits or risk being underinsured.

Property insurance companies rely on valuation appraisals to determine the amount of insurance for a particular building. Because reconstruction costs have increased significantly, the value of property being insured increases. Some insurers are mandating that associations provide updated replacement cost appraisals prepared by a certified professional appraiser. Increase in policy limits to account for increased cost of construction contribute to the overall premium increases.

Roof age is an area where carriers are constraining their ability to offer terms. For larger commercial structures near the coast, roofs older than 20-25 years tend to be unacceptable for the most competitive and reputable insurance providers. Commercial structures with older roofs receive unfavorable coverage terms including but not limited to roof coverage paid on an actual cash value basis as opposed to replacement cost, and roof coverage exclusions.

A leading cause of property claims is water damage due to frozen pipes and pipe breaks. Insurers have reacted by increasing deductibles, setting water damage limitations and even water damage exclusions. A large insurer for condominium associations will no longer insure associations taller than 4 stories due to unfavorable loss experience involving pipe breaks from higher floors causing damage to the units below. In an effort to mitigate this exposure and secure favorable insurance terms, associations should consider implementing water loss detection and/or automatic water shutoff devices throughout the structure(s).

Associations with a good loss history are facing increases in insurance premiums. Associations with adverse loss history face challenges to find insurance companies willing to offer coverage and can expect significant renewal increases.

Liability insurers are altering terms & limiting coverage as the liability market continues to experience difficulties driven by evolving social factors and increased litigation costs. Insurance companies are realizing increases in the number of claims at condos that have a high percentage of rentals. These claims include but are not limited to personal bodily injury, animal liability, and even claims by contractors performing work for associations and homeowners.

The excess liability & umbrella market continues to present its own challenges. Limited capacity in the reinsurance marketplace, as well as the increase in higher plaintiff awards being paid out with loss settlements continue to be the key drivers. Excess liability & umbrella carriers are reducing coverage limits offered, non-renewal of insureds with certain exposures, and significant pricing increases.

On a positive, the high interest rate environment has a positive effect on the property & casualty insurance industry. Most insurance carriers invest their reserves and surplus in conservative/low risk investments including bonds and low risk securities. The increase in investment income should help to offset the rising claims costs and rising reinsurance costs insurance carriers are experiencing.

If your association is facing significant increases in insurance costs, keep in mind that insurance markets fluctuate. Over the past 25 years, hard markets for coastal condominiums haven't lasted more than a few years. While this creates uncertainty in forecasting year-to-year premiums, a slow approach to raising condo fees in response to insurance increases may be prudent. Boards should communicate their strategy for financing significant increases in insurance premiums to association members.

The next column in this series will focus on identifying the right insurance agent for your association and how to avoid gaps in coverage.

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