

## Understanding the Homeowner Association Insurance Crisis

The Homeowner Association (HOA) industry is currently being impacted by radical changes being made by the insurance industry. The insurance industry has been effected by many factors that has necessitated these changes:

1. The 9/11 attack (at \$70 billion it is far higher than Hurricane Andrews' \$15.5 billion loss), increased claims (natural disasters have increased from \$7.5 billion in 2000 to \$11.5 billion in 2001), and the threat of future terrorist attacks has or will impact the insurance industries' assets.
2. The poor performance of investments made by insurance companies. In prior years, the income stream from a strong stock market has indirectly underwritten the cost of insurance.
3. The lawyer's focus on mold issues have increased mold claims from 48 cases in 1998 to 7,143 cases in 2001. To the litigation profession, "mold is gold." Expect to see more cases.
4. The building boom of HOAs occurred in the 1970s and 1980s, and therefore as a segment HOAs are getting older and are a higher insurance risk.

These factors have caused the insurance industry to reassess its HOA policies and take the following actions to mitigate their losses:

1. Everyone's liability and property insurance policies are being increased upon renewal.
2. New policy exclusions for terrorist attacks and mold repairs are being added upon renewal.
3. The insurance industry are performing on-site risk assessments of HOA facilities. They are looking for compliance with building codes, unsafe conditions, and the overall condition of the HOA facilities. The result of these inspections can result in a request for repairs and upgrades or termination of policies.
4. HOAs with above normal claims (multiple claims in one year or a history of claims) or mold risks (water related claims) are being dropped. This high risk classification can last until the problem is solved or during a probationary period of low claims for several years. High risk HOA insurance policies can be 3 to 4 times higher.

HOAs cannot be without insurance coverage. Lack of insurance will affect the sale-ability and value of HOA units and individual homeowners can be held personally liable in the case of a lawsuit. In addition, banks will not lend funds to HOAs that do not have insurance.

The following is a list of suggestions that HOAs can take to mitigate this crisis.

1. Raise the insurance deductible to \$5,000 or \$10,000. Many HOAs have deductibles of \$1,000 to \$2,500. This will reduce claims that could cause an HOA to be considered high risk and is a factor in the price of insurance.
2. If your HOA has not already received a risk assessment by the insurance company, we suggest that the HOA become proactive and request one.
3. Address suggested replacement repairs made by insurance company immediately.
4. Evaluate the need to submit specific claims on a case by case basis, considering the risk of increased insurance costs if the HOA was to be considered a high risk client. Based on the current environment, HOAs may need to consider themselves semi-self insured and save the insurance coverage for the "real" emergency. The insurance industry is no longer going to allow its policies to be used as an alternative source of repair funds. If an HOA make too many claims it may have to repay the insurance companies in much higher premiums.
5. A majority of HOAs have an underfunded replacement fund. Due to the importance of making certain repairs immediately and the lack of mold coverage on new insurance policies, many HOAs have to improve their effort to properly fund the replacement fund.
6. Mold repairs can be very expenses. HOAs need to mitigate future mold losses that its members will be required to pay due to the insurance industries new policy to exclude the cost of mold repairs from their policies. This requires a more proactive approach to assess the possibilities of water damage and to address these matters in a timely basis. HOAs need to consider the water damage risk due to poor roof, rain gutter, exterior painting maintenance and malfunctioning irrigation systems. The new criterion for replacement repairs needs to be the effectiveness of these components, not the availability of replacement funds or the expected remaining life of these assets.
7. Higher insurance costs may require revised budgets and/or higher or special assessments.