ADAPTING THE HO-6 TO COVER HIGHER ASSOCIATION DEDUCTIBLES

With the large number of weather related property claims in the past five years and with the dollar amount of claims far exceeding premiums, the pricing of habitational property insurance has skyrocketed; in some cases, the coverage has become unavailable. This development has adversely affected the finances of condominium and townhouse associations, which traditionally have insured the ownership interest of all unit owners under a single master policy. In the past two or three years, nearly all the major insurers who in the past have aggressively competed for these master policies have fled the scene. Only a handful today are open to new association business—and then only for very preferred risks (built in the last 20 years, no more than one or two claims in three years, roof recently replaced, no swimming pools, etc). Often, coverage for associations with an unfavorable loss history must be sought in the surplus-lines market, where rates can be 300% to 800% higher.

When faced with overwhelming cost increases, most associations, even loss-free ones, do the prudent thing – they raise their property insurance deductibles. The usual $1,000 deductible becomes $5,000, $10,000 or even $25,000. Not only do the higher deductibles reduce today's premium, but they also eliminate most of the small losses. Fewer losses reduce future premiums and protect the policy from nonrenewal.

If a master policy now has a $25,000 deductible, whose responsibility is it? The norm is for the unit owner(s) affected by a particular loss to pay for the master policy deductible. The association pays the deductible and assesses all members only when a loss affects all units; e.g., in event of a storm.

Read the agreements of your association. Make sure they are clear about who pays the association building deductible. If they aren't, point out that oversight to the association's board of directors. An HO-6 insurer will pay a master policy deductible under Coverage A only if the association's legal documents explicitly make the individual unit owner responsible for it. It won't pay the deductible just because you are getting billed for it.

Every association board that raises its master policy deductible should also amend the insurance section of the declaration document to specify under what circumstances the deductible will be charged against an individual unit owner(s) affected by a loss and under what circumstances the deductible will be assessed against all unit owners.

<u>Ten Steps to a Well Designed HO-6 Insurance Policy</u>

1. Request a copy of the association's "declaration" document. Make a list of building items not covered by the association's master policy (e.g., carpets, hardwood floors, tile floors, kitchen cabinets, plumbing and electrical fixtures serving the individual unit, built-in appliances, unit owner improvements.)
2. Estimate the replacement cost of all structural items that are your responsibility. (The easiest and most accurate way to do this is to write a list of all such items and then estimate the replacement cost of each.)
3. Ascertain the current master policy deductible as well as the maximum deductible authorized in the declaration. Choose the higher.
4. Add up the totals in Steps 2 and 3. Round up to allow for errors. That total should be the coverage limit for Coverage A.
5. Add "special perils" coverage to Coverage A, changing the perils covered from "Named perils" to "all risks" unless excluded. This is important for three reasons: You are covered for more losses (e.g., water damage to walls and ceiling from roof leaks), you have improved coverage for losses subject to the master policy deductible, and you broaden the HO-6's loss assessment coverage to special perils from named insureds.
6. Add special perils contents coverage (to cover damage to personal property from roof leaks, paint spills, etc.).
7. Add sewer backup and sump pump failure coverage. You want to do this for two reasons: first, to cover direct damage to the unit or contents from these two perils; second, to broaden the loss assessment coverage to include assessments for either peril. (Loss assessment coverage applies only to assessments for losses from perils covered by the HO-6.)
8. Determine the need for flood or earthquake coverage.
9. Recommend adequate liability coverage (e.g., $500,000) in limits equal to your other personal liability coverages.
10. Buy an umbrella policy. Be sure it includes coverage for association volunteer activities, including non-profit D&O, in case you ever serve on the board.