Lowenstein Sandler's Insurance Recovery Podcast: Don’t Take No For An Answer

Episode 78 -
Policyholders Beware: Maximizing Commercial Property & Casualty Insurance in a Steadily Hardening Market - Part II

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Eric Jesse: Welcome to Don't Take No for An Answer. I'm Eric Jesse, partner in Lowenstein Sandler's Insurance Recovery Group. Today I'm pleased to continue the discussion that we had on our last episode about the property and casualty insurance market. I'm pleased to welcome back Heather Weaver, who's counsel in Lowenstein's Insurance Recovery Group, and I'm also pleased to welcome back two insurance brokers who really know their way around the property and casualty insurance market, Josh Weisberg, who is the Chief Risk Officer at SterlingRisk. Welcome back Josh. Glad to have you here.

Josh Weisberg: Great to be back.

Eric Jesse: Great. And I'd also like to introduce our listeners to Brad Barron, who's partner and managing Deputy General Counsel at Conner Strong & Buckelew.

Brad Barron: Thank you. Great to be here.

Eric Jesse: Great. On our last episode, Josh and Brad really walked us through what the property and casualty insurance market is seeing, which is basically this increase to claim payouts for a variety of reasons, whether it's supply chain issues, inflationary issues, or just the seemingly increasing natural disasters and the cost associated with that.

Today what we want to talk about is, all right, now that we've identified the issue and the problem, how are the carriers reacting to that and what can policy holders do to come across as a good risk? Just to kick things off, Brad, can you talk about what are you seeing in terms of how the insurers are reacting to all the issues we talked about on the last episode and just the increasing claim payouts that they're having to make?

Brad Barron: Sure. I'll just talk a little bit about the commercial property market and what we're seeing in terms of how policies are being structured today. Which is, when you think about it, it used to be pretty much everyone had what was called blanket limits. You would have, let's say, a hundred million dollars of property insurance and even if you owned multiple buildings in different places, as long as any one loss didn't go over a hundred million, you were fine. Maybe your buildings were actually worth a little bit more than a hundred million, but the odds of all of them burning down at one time pretty low, so you would only get a hundred million dollars of insurance.

Now we're seeing more carriers, especially on the very large real estate property groups, either going with schedule by location, so you're getting 10 million for location A, 5 million for B, 10 million for C, or you're getting margin clauses in there, which are sort of similar, but saying, hey, you need to be within 10% of your declared value or we're capping out at what we're paying you. Even though you might have a total loss of a building that you thought was 10 million, like Josh talked about last time, the cost to rebuild that may actually be closer to 15 million now because of increased cost of labor, increased cost of raw materials, additional downtime.

Carriers are starting to constrict how you can build your programs, and we're also seeing an increased use of co-insurance. So that means no matter what your loss is, even if it is a partial loss and not a limits loss, you're still going to be responsible for 5%, 10%, 15%, whatever that co-insurance number is. That can have a big impact on you depending on how your program is structured and how dispersed your properties are, so still keeping in mind the commercial property market. One of the biggest impacts we see are places where you have a lot of buildings at one location. Is your policy limiting you by location or by building? What we would rather see is, hey, we want to a larger limit at a location because that gives us a lot more wiggle room because again, the odds of every building catching fire very low.

Those are some of the things that we're seeing driving this. In addition, we're also seeing, it's just, that we talked about last time, decreased capacity. So on these really large property programs, it's hard to build a tower of sufficient limits. Before it may take us 10 or 15 carriers to get to 500 million, now it's taking us 20 carriers to get to half that amount or 250 million just because reduced capacity and pricing.

You combine all that, you have insurance that costs more, you have more insurers involved, which means the likelihood that all the policies are going to be exactly the same is pretty low because some of them just will not agree to everyone else's terms, so you're going to have a little bit of a checkerboard perhaps of coverage, that's just the way it is in the marketplace. And then you're going to have these different limits, potentially, available at different locations. That's just a peek into what we're seeing. I know that Josh probably sees some similar stuff and maybe some additional things as well.

Josh Weisberg: I think that the limits issue is definitely a major driver of what we're looking at, what we're seeing and experiencing. Obviously, not on the flip side, but in addition to that is larger deductibles, larger deductibles for specific or specified perils. For example, an increased use of sublimits. What that basically means is using some of Brad's examples, you could have a property policy that gives you coverage for fire at a full building limit, let's say that limit is $50 million, but you could also have the same policy that says, I'll only cover you for water damage claims up to a million dollars.

Just so we're all on the same page here. What's a water damage claim? A water damage claim can be a lot of different things, but that could be a pipe burst. You could have, like we had experienced here in the northeast over Christmas last year, you could have arctic temperatures that cause a massive pipe burst within a building, those claims can be enormously expensive. Well, if the carrier has sublimited water damage to a million dollars, even if you had a $50 million policy, guess what? That loss is going to be adjusted up in about 30 days because all they're going to do is give you the million dollars and they're going to close their claim. We're seeing a lot of use of those sublimits.

We're also seeing a lot of use of increased deductibles for specific perils. For example, a named storm, we talked a lot about Florida last time, you'll see higher and higher deductible amounts in named storm related events in Florida. Like Brad pointed out before, there are different ways where that can be applied. For example, if the insurance company says, I'm going to apply the deductible for a named storm on a 5% basis, meaning 5% of the building limit, they can apply that 5% across the entitled property or they can even apply that 5% against each and every building at that particular location. The translation in terms of dollars when you start applying it on a per building basis can be absolutely enormous. We definitely did talk a lot last time about how price for insurance is going up, but at the same time the amount of coverage and the restrictions on that coverage are really starting to also bring a lot of pressure to the insurance marketplace for policy holders.

And it's a very dynamic issue. I mean, one of the things that we just saw only a few weeks ago, we were writing a risk in California where the insurance company was looking to outright exclude wildfire, meaning that they would not cover any claims associated with wildfire whatsoever. What makes that so incredible when you really take a step back, property insurance started with fire related risks. Fire was the genesis of property insurance historically, and now we have a circumstance where property insurers are saying, I don't want to cover particular kinds of fires. So that's a really dramatic illustration, in the world of insurance anyway, it's a very dramatic illustration of the kind of problems that we're facing right now.

Brad Barron: Go off what Josh was saying is number one, I think those of us who live this life know the property policies are all different. Unlike your general liability policy, you're dealing with each carrier's different policy form. So it's sometimes difficult to really be able to compare insurance company A's policy to insurance company B'S policy because they're all going to operate a little bit differently, define things differently, different sublimits, all that sort of stuff.

One of the things that Josh was mentioning about wind and named storm that's coming up as well and that we're seeing is some carriers are giving you a sublimit that is a percentage of your statement of value. So you're declaring, hey, this building is worth $10 million. And they're going to say, okay, for wind or named storm, I'm going to give you 10% of that. Other carriers are giving you a percentage of the replacement cost value, which you don't know what that is until the building has to be rebuilt. So that leads to sometimes a lot of uncertainty. How much am I actually going to get should this peril happen? It's just adding in some more question marks, and it makes it harder and harder to really be able to compare apples to apples sometimes when it comes to these different property policies and programs that are out there.

Josh Weisberg: And I would add to that, it's another really rock-solid example of some of these challenges, we see a lot of carriers now, particularly on roof damage related to any kind of barrel, depending upon the age of the roof, they will no longer offer full replacement costs for that roof. For example, if there's a windstorm that tears off a roof that's 10 years old, they'll only give you the actual cash value of that roof at the time that the loss occurs. For example, again, if it's a 10-year-old roof, that's a roof that's probably worth, let's say 10,000 bucks, it's going to cost you 60,000 bucks to replace it. Guess what? You've only got $10,000 worth of coverage. It really does perfectly illustrate what Brad's talking about.

Eric Jesse: You've both raised very good points and it's obviously a difficult market. As you're talking about different policy forms, Josh, you talked about water are damage, what is water damage? Brad, you talked about limits on a per location or per building basis. I mean, these are all just, I think, cautionary tales for our clients, for policy holders that they need to understand, number one, the words on the page truly do matter, which is one of our themes here on Don't Take No. And that policy holders really need to go into this eyes wide open because, Josh, when you gave the example about $50 million limit, but a $1 million sublimit for water damage. So number one, what is water damage is going to be critical depending on the event an insured is facing. And we certainly saw that with Hurricane Sandy. Was it a flood or was it-

Josh Weisberg: Wind-driven water? Or was it the mysterious fire that consumed the building right before it was going to get knocked over?

Eric Jesse: Exactly. Is the damage caused by the rain or from the flood? And these are issues that have multimillion dollar implications, so it's just important for clients to really understand and to be eyes wide open. But I guess that maybe begs the question, once clients are eyes wide open and they do see what is in their policy and they don't like something in their policy, where can there be pushback? Or where is there room for negotiation with the carriers? Are any of the things you're talking about set in stone or is there room for negotiation?

Josh Weisberg: I would say that the short answer is that sometimes there is room for pushback. In the underwriting process, in many circumstances it is about negotiation. That's why your broker is there. Your broker is there to advocate for you to get the best possible pricing and the best possible coverage. But just using one of the examples that Brad was talking about before margin clauses. Those margin clauses are set at specific percentages. We have found that you can push back on those percentages. You may not be able to get margin clauses completely eliminated from your pricing terms, but you can look to bump those percentages to try to give yourself extra protection in the event that you're going to need to access the policy for a claim. That's just one area. Just one example of the things that you can do to really try to push.

I would say that if you're looking to exert leverage to try to improve policy terms, and I'm sure Brad would agree with me here, the best way to position yourself in order to capture those improvements is to talk to your broker, to talk to your insurance advisors, to talk to your outside policyholder council advisors early on. If you really want to prepare yourself for these kinds of events, don't wait until 30 days before your insurance is supposed to renew. Before you start having these conversations, start pressing your broker, start pressing your insurance advisors, I need to know what my policy terms are going to look like so I can really start carefully scrutinizing them and I can understand where are my exposures, prioritize those exposures and push for improvements in policy terms where I know I have the greatest exposure to any one particular loss. That's huge.

And the other piece of advice that I constantly give my clients is, don't just worry about the actual terms of coverage and the actual premium. Where you really can affect a difference is when you present yourself to the marketplace as a best-in-class risk. When we talk about that, what really mean is, from a risk management standpoint, talking again about water damage, do you have what's called a water mitigation plan? Can you show your insurance company, or the marketplace in general, that you have a written plan that you're going to execute on in the event there is a pipe burst? That you know how to shut off the water. It can be just as basic as that. Just one example of something that you can show underwriters that you have in force to make you look like a better risk, and that doesn't just again, translate into lower premium potentially. It also translates into better price. So instead of having that 1 million water damage sublimit, you might be able to increase those sublimits to get yourself better coverage.

Heather Weaver: Josh, you mentioned getting involved with your broker early and getting those discussions started. Is there anything else that policy holders can do in advance of the underwriting process internally, maybe on the business side to assist with the underwriting process to be prepared for the underwriting process in order to achieve the most favorable policy terms at the most reasonable rates possible?

Josh Weisberg: I mean, I'd be interested to hear what Brad asked to say on, it's a great question, what Brad asked to say on that. It definitely does speak to what I was saying before, which is, in advance of renewal and really during the entire policy term, you should be thinking about what risk management strategies do I have in place to make my property the safest risk possible? We talked a little bit about water are damage mitigation plans, fire mitigation plans, the right contracts with vendors. That's always a very critical aspect when an insurance company is reviewing your account. They want to make sure that if you have an elevator vendor that provides elevator maintenance, they want to see great contracts that are going to show that elevator vendor is going to protect you in the event of a loss, that they've got good insurance, so that if heaven forbid there's a loss, they know that the elevator contractor is going to be responsible for any of that loss or damage. That's absolutely huge.

They also like to see specific safety steps or measures related to security. Negligent security claims are a huge issue these days. So if you can show a potential insurer that you've got exterior floodlighting, if you can show them that you have outside security vendors that patrol your locations, all of that shows that you're an attractive risk and they want the attractive risks because they have, obviously, they have less exposure to claims with better risks in the marketplace.

Brad Barron: I agree with Josh. I think risk management is a huge piece of it. Another thing that we see some insureds struggling with is updating their records. And by that I mean when was the last time you had someone identify what your statement of values were? How much is it really going to cost to fix your building in the event of a fire, a flood, whatever, so you get the right levels of insurance. Because that's going to be a critical question, you're going to be getting what's the value of this stuff, whether it's your machinery, the actual building envelope itself.

The other thing that we're seeing people ask about, and we've touched on it previously, was business interruption. Huge piece of coverage here. What happens when I go down? Or contingent business interruption? What happens when one of my key suppliers goes down let's say? We're seeing more carriers ask questions about what does your supply chain look like? Who are those vendors? We want to have a list of them, and in some instances, we're only going to cover you if it is a vendor on that list that goes down or something of that ilk. So really understanding your business.

Knowing what the risks of your vendors are. Have you done the due diligence? Have you almost done what Josh is talking about, but for your vendors? Especially the really, really important ones. The one that you're getting the key widget from, have you been out to their factory? Are you satisfied that they have redundant policies in place and procedure should something befall them? I think all that stuff and really getting started early, like Josh said. Every second, especially as you get closer and closer, really fraught with all sorts of questions, so the earlier out you can answer a lot of those questions and have that information at your fingertips gives you the best chance at being one of the people who gets that better set of rates and conditions and policy forms.

Heather Weaver: These are some really helpful practical tips. Thank you for that. Looking into your crystal ball as we often like to do on Don't Take No, Josh, where do you see the property and casualty market going over the next few years?

Josh Weisberg: And Brad, you can absolutely jump in here and tell me if I'm wrong. We are in what's called a historically hard market. This has been one of the longest hard markets, if not the longest hard market, that we've had in recent memory. And by hard market, all we really mean is, premium is going up quarter over quarter, and coverage terms are becoming more and more restrictive. Some of that has to do with increased interest rates, all the drivers of premium costs that we talked about during the last episode.

I don't foresee rates continuing to increase at the percentages that we've been seeing over, let's say, the last four years. I think you're starting to see some arresting in the rate of those increases. However, I don't believe that we're going to be looking at any sort of material reverse trending, meaning that when it's all said and done, we are likely to remain in either a hard market or a pseudo hard market for some time now, which is why all of these steps that we're talking about are so critical because that's how you're ultimately going to be able to contain loss. That is the way that I see it. Brad, tell me if you think good, bad, indifferent, what do you-

Brad Barron: No, no. I agree. I'm not quite as brave in terms of making prediction about price. I'll make a prediction about the process though. My prediction is that it's going to become more painful for policy holders because I think insurers are going to want more and more data. They're becoming a more and more data-driven enterprise. If we just talk a second, flip back the page a second to contingent BI, who are your vendors? They want to know that because they want to know where your vendors are located so they can see, okay, do I have a huge concentration of vendors and business interruption type of exposure beyond my actual insured? They're going that extra level.

I think it's going to happen that they're going to start quasi underwriting those people as well, as part of your risk to know what the exposure is for your business interruption. So I think they're going to ask more and more questions, more and more questions about your business, how it operates and that sort of stuff, because they really want to try to get as granular as possible so they can make sure the risk is spread appropriately and priced appropriately. That's my prediction. Many times, wrong before. We'll see.

Josh Weisberg: That's probably a safer prediction than mine, but I think... What I would say is this. The honest truth is, Heather, just to answer your question, what's the reality? The reality is that these predictions are irrelevant, and the reason why they're irrelevant is, to Brad's point, you're not going to really be able to control what happens in terms of pricing within the insurance marketplace. As we talked about last time, there are so many different drivers of what ultimately translates into cost for insurance. Control what you can.

Brad did a good job of talking about what those control factors look like, I outlined a bunch of what those control factors look like as well. You're not just looking at the four corners of the policy. Don't just look at the four corners of what your coverage terms are. That is critically important. What's also even more important is trying to position yourself where you're never going to have to access your insurance policy. Do what you can to avoid claims, talk about a lot of the steps, implement the steps that we're talking about, develop them even further, and you're going to be in the best possible position to handle a soft market, a hard market, a middle market, whatever it might be, that's how you control costs the best of your ability.

Eric Jesse: No, Josh and Brad, thank you for your insights. I was going to say that given your crystal ball predictions, what policy holders need to do is really just be very mindful of insurance. They can't just take their insurance policy and put it on the shelf. They need to be thinking about it. We're just in a situation where they need to be constantly thinking about it and how they can be a good risk. What are the terms and conditions? What are the preventative measures or steps that they can take to assist in the underwriting process? I was going to say that that applies because of the hard market. But Josh, you make the good point that policyholders should always be mindful of these things, even if it's a soft market.

Appreciate your insights on your crystal ball predictions, but also just appreciate the practical tips that you've given here. Thank you all for joining us on Don't Take No for An Answer. We appreciate it.

Josh Weisberg: Thank you.

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