



## INSURANCE FOCUS

### CONTROL LOSSES IN INDIVIDUAL UNITS

Controlling property losses in individual units, especially in the areas of fire and water damage, is an essential part of community association management. Loss prevention and mitigation of damages are keys to managing community association insurance costs. Loss history is of great concern to insurance company underwriters, especially with large numbers of small losses. The community association that can show an insurer a serious effort at pinpointing potential risks and controlling exposures, such as by eliminating or transferring them, makes a better underwriting impression.

#### Why is loss control important?

It is vitally important that community associations make every effort to control claims. Each incident should be evaluated to determine whether a claim to the insurance company should be made. In many instances, it may be better for the community association to pay for the loss, rather than make a claim, as many claims may lead to increased insurance rates or dropped coverage altogether.

#### Why is water control important?

Research by USI shows that water damage is by far the highest cause of loss, comprising 44 percent of the total incurred and fire accounts for 29 percent, and falls account for 5 percent. Six types of claims cause 68 percent of all water damage:

- plumbing pipes (19 percent);
- AC/water heater (15 percent);
- toilet (10 percent);
- external drain (9 percent);
- internal drain (8 percent); and
- wind driven rain (8 percent).

#### What can we do to prevent losses?

In order to prevent losses and save your community association money, consider implementing the following solutions:

- monthly or quarterly air conditioner and condenser inspections in all units;
- annual sewer and drain inspections and repair; and
- annual inspection and repair to roof, siding, windows, and skylights.

#### What should be done in individual units?

Individual units contain several potential sources for leaks, including washing machine hoses, ice maker lines, HVAC units, water heaters, and dishwashers. Residents should check periodically for signs of potential water problems. Inspect all exposed pipes for leaks, and check all faucets for leaks or corrosion. Equip showers, sinks, and tubs with drain screens to catch the debris, hair, and bits of soap that can cause clogs and back-ups.

Inspect the rubber connecting hoses for dishwashers and washing machines. Contrary to what some believe, such hoses do not last forever. Because these hoses wear from the inside out, a visual inspection will usually not reveal any worn spots. Some higher quality machines will have longer lasting burst free hoses, but for the most part, these hoses should be replaced every three to five years, or sooner if evidence of rot appears.

The major source of property and insurance loss is water-related and occurs “behind the door”—inside the owners’ units.

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The Institute for Business and Home safety reports that water heater failures continue to be one of the top five sources of residential water losses for the insurance industry, costing an average of \$4,400 per incident.

Recommended maintenance includes two steps. First, have a professional plumbing inspection of the anode rod at least once every two years and annually once the warranty has expired. The rod will eventually corrode and leave the tank vulnerable to damage. Second, remove sediment by flushing the tank every six months. Sediment will build up faster in areas with hard water. Please see the "Ask the Expert" column for more information on inspections and maintenance in individual units.

### What if water damage occurs?

If water damage does occur, unit owners should report the incident to the community manager to ensure everyone's safety and to minimize damage.

Keep in mind that the longer water and humidity are present, the more damage will result. Determine the source of the water and turn it off. Residents should know the location of the individual shut off valve located in the unit, if there is one, and how to use it.

Remove furniture, rugs, and any other covering from wet carpet or the floor, and lift draperies so water does not move onto the fabric. Then concentrate on drying out the structure. In the summer, the air conditioner will need to be on with windows closed to reduce humidity; in winter, maintain a

temperature of 70 degrees and crack windows open. Fans will help move air around and decrease humidity.

The services of a professional may be needed. Water will gravitate under walls, carpets, and under insulation in walls. Use caution when turning on overhead light switches, as water could be in ceilings, which could result in an electrical fire.

If the sewer has backed up, professional help should be sought because of the possibility of contamination. Finally, have estimates prepared for

Alarm systems, smoke detectors, and sprinkler systems must be tested on a regular basis, and records should be maintained. Also, smoke detectors should be battery-powered and hard-wired so as to operate in the event of either battery failure or central panel power failure.

Individual units should have smoke detectors outside each bedroom and on each level of multi-story units. The smoke detectors should be tested monthly, and the batteries should be replaced at least once a year or when they make a "chirping" sound.

The kitchen is the number one site for home fires. Kitchen fires frequently result from food, grease, or combustible materials left on stove-tops. A fire extinguisher should be located in the kitchen, and household members should be taught to use it.

### What about electrical systems?

Maintenance must be

performed on schedule, and a licensed and insured electrician should be consulted to make any corrections needed. A building inspector should look for:

- electrical outlets or devices that are hot to the touch;
- loose wiring;
- wiring touching beams or nails;
- old, badly corroded metallic tubing;
- excessive extension cords;
- heat-producing devices mounted too close to combustible materials;
- flammable items stored too near panel boxes or transformers; and
- the correct size breaker for the job.

## QUESTIONS TO ASK

Would a community association master policy or a resident's personal policy provide coverage if...

- A fire breaks out in an adjoining dwelling and destroys a wall between the units?
- A fire breaks out in an adjoining dwelling and causes smoke damage but no actual destruction of property?
- An adjoining dwelling experiences sewer back-up?

Answers to these questions will depend on the type of insurance coverage obtained by the community association.

structural damage one to two weeks after the incident. Frequently, damage is not apparent immediately but appears after the structure dries out.

### What should we know about fire prevention?

Smoke alarms and automatic sprinklers have made fire damage preventable to a large extent. Smoke alarms and automatic sprinklers are frequently mandated by law, and most new buildings are constructed with fire walls, fire doors, and non-combustible materials. Problems arise when maintenance becomes lax.



### What will insurance cover?

Individuals who live in a community association may assume they and their possessions are covered against loss by the association's master policy. Usually, this is not the case. A community association must provide insurance coverage against typical hazards and perils that might affect an individual owner of a residence, but this coverage does not usually extend to unit owner's improvements and betterments, personal property, or personal liability.

The most common type of master property insurance purchased by community associations is "single entity" coverage, which insures the general common and limited common elements. This coverage also extends within individual units to fixtures, appliances, walls, floor coverings, and cabinetry, but only for like, kind, and quality to that conveyed by the developer to the original owner.

In other words, building coverage under the master policy in this type of policy is limited to the original plans and specifications. Any individual unit improvements made subsequent to the original conveyance, such as building a wall to divide a room, or upgrading carpeting or other floor coverings, wall treatments, appliances, cabinetry, etc., are not covered by the master policy. These improvements are the responsibility of the unit owner to insure.

### Who should pay the deductible?

It is important for the community association to determine who is responsible for paying the deductible. For instance, if a fire starts in a unit, who pays: the association or the prop-

erty owner? The question of who pays the deductible can be answered in at least five ways:

- 1) The property owner who suffers the damage incurs the cost of the master policy deductible.
- 2) If a negligent party causes the damage, the negligent party incurs the deductible cost.
- 3) If the association must pay the deductible, it may be paid out of the operating account or an operating reserve account if the association has one set up.
- 4) The association will make a special assessment for all master policy deductible claims on an annual basis.
- 5) The owner of the unit from which the cause of loss originates pays the deductible. If the cause of loss originates from the common elements, the association pays the deductible.

*It is important to note that responsibility for the master policy deductible might be dictated by the association's bylaws or state statute in some cases.*

### What should residents do to protect themselves?

Residents must be aware of the type of coverage in effect through their community association. Regardless of the kind of policy a community association has, owners and tenants should purchase a personal policy to fully protect their interests.

Resident owners should consider purchasing an individual Community Association Unit Owners policy (HO-6). This policy can provide coverage for personal property, unit improvements, betterments, additions and alterations, additional living expenses, personal liability, loss assessments and damages less than the master policy deductible. Non-res-

ident owners may not need coverage for personal property or additional living expenses; however, they do have all of the other insurable exposures of a resident owner. Additionally non-resident owners can be insured for loss of rental income. Renters should purchase a Tenants Homeowner (HO-4) policy to provide coverage for personal property, additional living expenses, and personal liability.

Coverage can be arranged under some HO-6 policies to pay for damages to a unit over the personal policy deductible, usually \$250 or \$500, up to the master policy deductible. This type of coverage is generally referred to as "building" or "dwelling" coverage under a personal homeowner's policy. Unit owners should check with their HO-6 policy agent or the insurance company to determine if they have appropriate "building" or "dwelling" insurance to cover damage to their unit up to the master policy deductible.

The master policy will not cover personal property, such as clothing and furniture within individual units, nor will it provide coverage for personal liability or additional living expenses.

Homeowners must be aware of current market conditions and of the type of coverage in effect through the association. They need to understand that deductibles have increased, which could result in a significant out-of-pocket expense without the appropriate personal insurance protection.

### Where can I get more information?

If you have any questions or need further information, please contact Steve Dickerson (703-205-8788 or Steve.Dickerson@usi.biz) or



ASK THE EXPERT

“Ask the Expert” is a regular column in Insurance Focus, featuring an interview with an expert about an important insurance issue facing community associations. This month our expert is Thomas L. Willis, PCAM, Vice President at Zalco Realty, Inc. He is a frequent presenter and instructor for the Community Associations Institute and a two-time winner of the “Educator of the Year” Award for CAI’s Washington Metro Chapter. He also formed Association Bridge, LLC to provide consulting services to community associations and businesses. Tom can be reached at twillis@zalco.com, associationbridge@gmail.com, or at (240) 372-0905.

**Q:** Can and should community associations conduct routine inspections and maintenance on individual units?

**A:** An in-unit inspection and maintenance program can bring huge benefits to community associations. But a careful analysis of each situation is in order to determine if and how a program should be undertaken.

Condensation drain line back-ups can result in thousands of dollars in damage. Leaky valves left unattended may result in the need for mold remediation. Burst washer hoses and rusted out water heaters could easily result in a significant master policy claim. One faulty smoke detector can result in injury or, worse yet, loss of life.

Can associations prevent such things from happening? Of course not. But a systematic in-unit inspection and maintenance program can go a long way to avoid or mitigate them. This may be an opportunity to prevent damage, control expenses, contribute to quality of life, and add value to association membership.

**4-Point Analysis**

1. Risk Management Analysis—Component Wxposure: What are the elements in units, what damage could those elements cause, and what are the potential soft and hard costs of that damage?

- 2. Risk Management Analysis—Property Configuration: A single family HOA? No way. A high rise condominium with a central HVAC plant and fan coil units? Nearly a no-brainer.
- 3. Resources: What are the capabilities of on-site staff? Are contracted services an option?
- 4. Legal Considerations: What is the association’s authority per its governing documents and prevailing law? What liability considerations exist? Review with association counsel.

**Why Not “Risk Management Inspections?”**

Why stop at the standard seasonal filter change program? Why not use this as an opportunity to address other conditions to raise awareness of potentially problematic conditions and assist unit owners to fulfill their duty to maintain? The list should include everything from tub grout to smoke detectors.

**Implementing the Plan**

- 1. Using the 4-Point Analysis, decide on the intensity of the program. It could be anything from inspections followed by notice to inspections plus maintenance.
- 2. Document the program as a policy (legal assistance is strongly recommended), and include inspections list and procedures.
- 3. Communicate, communicate, communicate the plan and its implementation, always highlighting the reasons for, and benefits of, the program.

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