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NATIONAL AFFORDABLE HOUSING MANAGEMENT ASSOCIATION

Ensuring NAHMA Members Receive the Latest News and Analysis of Breaking Issues in Affordable Housing

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NAHMA Survey Results: Property and Casualty Insurance Premium Cost Increases and Availability Issues

Effective Date or Deadline

The information in this NAHMAnalysis is derived from a survey of NAHMA and AHMA members which was conducted from November 3 through 20, 2003.

Background

During 2003, NAHMA received numerous reports from its members that they were experiencing last-minute cancellations or significant increases in their property and casualty insurance premiums – notwithstanding the historically low losses and the well-maintained and often-inspected nature of their properties.

In the fall of 2003, the Affordable Housing Management Association of Washington (state) filed a letter of complaint with the regional Office of Fair Housing and Equal Opportunity (FHEO) on behalf of its members. As noted by AHMA Washington Executive Director Joe Diehl in a memo to members dated Oct. 24, 2003, "We asserted that the last minute cancellations of property and casualty insurance, and the escalation of premiums – sometimes over 400% – represented a form of 'redlining' by the insurance industry against affordable housing operators. Our collection of information from our members indicate a loss history of 37% – far below what would be necessary to justify either cancellation or any increase in premiums."

According to Diehl, the regional Office of FHEO has opened an inquiry based on the AHMA Washington complaint.

In addition, the Washington AHMA and several other nearby AHMAs have launched an effort to provide specially quoted group property and casualty insurance to their members. For more details, visit the Washington AHMA website at http://www.ahma-wa.org/.

Meanwhile, to better establish any evidence of national trends in property and casualty insurance cancellation and/or premium increases, NAHMA undertook its survey of members in November 2003.

In considering the findings of this survey, members should understand that the results should **not** be considered the “final word” on the issue of property and casualty insurance premium increases and/or cancellations. The survey was an informal, first attempt to gather nation-wide information on this problem. The results should be interpreted with caution. This survey was not conducted in accordance with scientific research standards. Responses are based on self-report, have not been independently verified by NAHMA and are often the best estimates of the respondents. For all of these reasons, the results summarized below should be considered approximations.

Despite the scientific shortcomings of the survey, it has served a very useful purpose. The survey suggests that significant increases in property and casualty insurance have been experienced by many affordable housing providers across the country in the past year. Of the 123 properties that completed the survey, 56% had experienced property and casualty insurance premium cost increases of more that 41%. Also, 44% of the respondents had received a notice of cancellation before the expiration of their property and casualty insurance policy.

Summary

The survey was sent on November 3, 2003 to NAHMA members and the AHMAs, and the closing date was November 20, 2003.

The survey was designed for completion by single properties, and received 123 responses. In addition, some members with large portfolios of properties provided general comments on their overall experience, rather than complete the survey for individual properties. A copy of the original survey form is attached at the end of this NAHMAnalysis. (Some respondents did not answer all of the questions in the survey, thus, each question does not necessarily have exactly 123 responses.)

Survey Results

***Property and casualty insurance cost increase and cancellation problems exist across the country.**
The 123 respondents to the survey represented properties in 21 states, as follows: AL–1, AR–3, CA–1, FL-22, GA-3, IA-3, KY-4, LA-1, MA-1, MD-1, MO-3, MS-5, MT-1, NC-31, NE-2, NJ-6, PA-1, SC-6, TN-17, UT-1, VA-9. (One property provided a city rather than state location.)

***Most respondents (85%) represented properties with less than 200 units.**
Respondents reported their property size by number of units, and the percentage breakdown is as follows: under 50 units-21%; 50 to 99 units-32%; 100 to 199 units-32%; 200 to 499 units-10%; 500 to 999 units-1%; 1000 to 1999 units-2%; 5000 to 9999 units-1%; 15,000 to 22,000 units-1%.

***Most respondents (78%) represented affordable housing for families.**
Survey respondents indicated that 78% represented Family properties, 19% represented Elderly properties, 2% represented Family and Elderly properties, and 1% represented Disabled properties.

***Most respondents (70%) represented properties over 21 years in age.**
The percentage breakdown of the properties represented in the survey is as follows: under 6 years old-5%; 6-10 years old-3%; 11-15 years old-2%; 16-20 years old-18%; 21-25 years old-31%; 26-30 years old-16%; over 31 years old-23%; various ages-2%.

***A notice of cancellation of property and casualty insurance was received by 44% of respondents.**
In addition, a number of properties in North Carolina reported that the notice of cancellation (which had come midway through the term of the insurance policy) was withdrawn after complaints were lodged that the cancellation represented a possible FHEO violation.

***Most cancellation notices were sent with a 60-day notice period.**
Of respondents who had received a notice of cancellation of property and casualty insurance, 69% reported that they had received a 60-day warning as part of the notice. Other notice periods reported were as follows: 30 days or less-8%; 45 to 59 days-8%; 90 to 120 days-13%; more than 120 days-2%.

***Most respondents who had received a notice of cancellation of property and casualty insurance did not receive a written reason as to why the cancellation had occurred.**
38% reported that they had received no written reason as to why their property and casualty insurance was to be cancelled. Of the few reasons that were cited, the breakdown is as follows:
- The property contained aluminum wiring, and thus was not eligible for insurance – 12%
- The insurance company is not providing that type of coverage any longer – 4%
- Cancellation was due to overall catastrophic losses in the state (FL) – 4%
- The insurance company didn’t insure “subsidized housing” – 1%
- The balance of responses were unique or very specific to the property, or were blank or “n/a”

***A majority of respondents (56%) had experienced an increase of 41% or more in the cost of their property and casualty insurance premium.**
The reported increases in premium costs are as follows:
0 to 10% increase – 2%
11 to 20% increase – 1%
21 to 30% increase – 5%
31 to 40% increase – 3%
41 to 50% increase – 8%
51 to 60% increase – 18%
61 to 70% increase – 13%
71 to 80% increase – 5%
81 to 90% increase – 0%
91 to 100% increase – 0%
101 to125% increase – 3%

126 to150% increase – 1.5%
151 to 200% increase – 2%
201 to 250% increase – 1.5%
251 to 300% increase – 1.5%
301 to 499% increase – 1.5%
500% or more increase – 1%
Don't know – 2%

However, 8% of the respondents to this question noted that their property and casualty insurance premium had *decreased*. The range of decreases in premium costs was from 2% to 25%, with the average being 12%.

In addition, some 20% indicated they had been able to find equivalent replacement insurance once they had received notice of cancellation or significant premium cost increase, while 3% reported that they had still not found replacement insurance at the time of the survey.

***Many respondents (40%) also increased their deductible to make the insurance a little more affordable.**
4% of respondents noted they had already increased their deductibles at an earlier time, and several others noted other changes they made in their policies, such as mold exclusion and a reduction in coverage.

***Most respondents (71%) plan to adjust for the increased insurance premium by cutting other expenses in their operating budget.**
The reported methods for dealing with the increases in premium costs are as follows:
- Reduce other budget items/cut other operating expenses – 71%
- Increase rents – 15%
- Borrow from replacement reserves or residual receipts – 4%
- Combination of cutting expenses, increasing rents, borrowing from reserves – 3%
- Don't know how will cover the increase – 2%
- No answer – 5%

Two quotes representative of the responses are provided below:
"How can we cover the increased premium? Our rent increases are no where close to the increase in premiums. We have to look for other expense areas (where we are already thin), but essentially we have to eat it."

"The year we were cancelled was 2001, during the next two years we have experienced 30% increases each year. We have absorbed through careful budgeting and COA rent increase from HUD. Trying to budget and absorb the increases just take away from property repair needs."

***Most respondents reported that 0 claims had been filed with their property and casualty insurance carrier for each of the preceding five years:**

Year 2003:
0 claims – 80%
1 claim – 14%
2-3 claims – 4%
4-5 claims – 1%
6-7 claims – 0
8-9 claims – 0
10 claims – 1%

Year 2002:
0 claims – 68%
1 claim – 18%
2-3 claims – 8%
4-5 claims – 2%
6-7 claims – 0
8-9 claims – 1%
10 claims – 0
n/a – 3%

Year 2001:
0 claims – 64%
1 claim – 24%
2-3 claims – 6%
4-5 claims – 1%
6-7 claims – 0
8-9 claims – 1%
10 claims – 0
n/a – 4%

Year 2000:
0 claims – 68%
1 claim – 13%
2-3 claims – 10%
4-5 claims – 1%
6-7 claims – 2%
8-9 claims – 0
10 claims – 0%
12 claims – 1%
n/a – 5%

Year 1999:
0 claims – 68%
1 claim – 15%
2-3 claims – 9%
4-5 claims – 3%
6-7 claims – 0
8-9 claims – 1%
10 claims – 0
n/a – 4%

***Miscellaneous general comments from survey respondents:**

1) "[Our company] has almost 78 locations in a 'pool'. At our 9/1/2003 renewal we saw an average increase of approximately 4% overall. This is compared to the 9/1/2002 increase of approximately 45%. We believe the market has gotten over the significant correction in 2002 and will increase on a more modest pace in the future (barring unforeseen catastrophes)."

2) "We have since found a large master policy that our conventional properties are included in. We do not have a problem with our subsidized properties being accepted from a hazard/property insurance standpoint, but from a GL standpoint, we cannot gain acceptance into the master program. The carrier last year was [Name] and this year is [Name]. Both have policies that prohibit insuring affordable housing. I have tried to argue till I'm blue in the face with our insurance agents. They say they understand, but that it is the underwriting policies of the insurance companies. Our agent for the Master policy told me, separate from our other insurance agent who told me more than a year ago, that the head of [Name], absolutely forbids any type of subsidized housing - that he personally makes it an issue. To me, I think it is a form of discrimination. They are making judgments based on stereotypes of individual classes, races, age, and so forth. Really is terrible. I might add, I have lower loss runs for affordable housing properties than I do market rate/conventional."

3) “We had a very difficult and stressful time securing new P/L insurance for our buildings. No one wanted to insure us due to our location on the coast of [State]. We finally were able to obtain coverage at a considerable increase.”

4) “Many of our properties have received incredibly high increases over the past three years, beginning prior to 9/11/01. It has been explained to us that the habitational market and wood frame buildings are not desirable. We have been told that many insurers are getting out of this line, and we have seen the number of markets refusing to quote. This also affects our condo markets—not just low income. One insurer has flatly declined to quote Section 8 properties, while in fact they were insuring a Section 8 property we retained as a client a couple of years ago. They did inspect several of our properties and consented to insure another of our properties in [State] because it was in such good condition. It had rates less than the expiring.”

5) “In 2002 we had a large hail damage claim and were dropped by [Name] Insurance Co. We couldn’t find another carrier and had to accept a bid from a company on the secondary market with our premium going from $5,479 to $31,465.98 with a $2,500 deductible. Since that date our State Rural Development office suggested [Name] from [state], and we presently have our insurance with them for $20,740. We are hoping to keep claim free for 3 years so we can possibly get a lower rate.

“In the process of trying to find coverage we received a very interesting letter from an agent at the [Name of company] which I am attaching.”

Excerpt from attached letter referenced in preceding paragraph:
“Unfortunately, at this time we do not have a standard market for your property and liability insurance. Presently, our standard carriers are not writing any senior housing facilities which do not incorporate some level of assisted living; providing assisted living allows for state licensing which incorporates a greater level of resident requirements. In recent times, companies have seen fully independent senior housing facilities (whereby residence is based upon age and income level) challenged in court by various “fair housing” acts. The result has been an increase of student, unemployed, and or other low income residents ‘infiltrating’ these facilities (due to court decisions which do not allow for individuals to be discriminated against on age alone). Therefore, the final product has often become a low-income housing facility that is rarely run and maintained as well as initially intended.”

6) “We have almost all of our portfolio, some 130 sites, in one giant package policy. The premium increases the last two years have been very modest, 5% or so this year (Nov to Nov is our policy year), about the same last. We have boosted Terrorism coverage, we have coverage for mold, and we have no FEMA tier 1 properties. Our rate per $100 is extremely competitive with the largest REITs and our deductibles are $1,000 or $5,000 depending on property size. So all in all we are in very good shape, and have had no problem at all adding new management accounts to the policies. We have the sort of claim activity you would expect; a dozen or so fires a year, mostly small, but one took out most of a building. We did have some buildings get clobbered in the recent hurricane. Some liability claims, and a few lawsuits working at any given time. It is important to note that the new product we are involved with building or rehabbing, some dozen jobs altogether, are all being sprinklered (yes even the frame construction ones), and

have pretty aggressive loss mitigation designs. We actually have carriers coming to us wanting to bid on our business again, in contrast to last year."

Issues of Concern to NAHMA

NAHMA is extremely concerned about the very high increases in property and casualty insurance premium costs reflected by the survey responses, and the impact these increases likely will have on the ability of agents and owners to run well-maintained affordable housing properties within balanced operating budgets, with little to modest rent increases.

A second concern is that the majority of properties reporting high insurance costs in the NAHMA survey represent communities most likely to have difficulty in absorbing the new high costs, or in finding a new carrier. Based on the demographics of the survey respondents, most of the properties represented were small (85% had less than 200 units), family-oriented (78%) older properties (70% over 21 years in age). In contrast, the comments provided by several large NAHMA members reported relatively modest property and casualty insurance cost increases in the past year. This contrast adds support to a hypothesis that it is the smaller, older family properties being most severely affected by escalating property and casualty insurance costs. (However, this concern remains a hypothesis in analyzing this particular survey, in that it was not conducted in a scientific manner, since the results reflect the experience of those who chose to respond, rather than a statistically valid sample.)

An insight to this hypothesis is provided by NAHMA members who have reported talking "on background" recently to insurance carriers and brokers who work in the habitational markets. These members reportedly have been told that the least profitable and most expensive to serve insurance markets are smaller, older frame construction multi-family residential buildings. It was shared that some underwriters have said that these "risks" (policies) are perceived to be the least likely to be with owners and operators who have good loss mitigation and risk management practices; the properties are single asset entities; and often may be thinly capitalized. NAHMA members have also heard from several sources that owners who move from carrier to carrier to pursue the lowest price in all cases are seen as less desirable business partners over time. Reportedly, changing carriers in the past is taken into account on renewal decisions.

Thirdly, we are concerned by the several comments by respondents that reflect perceptions that some of the property and casualty insurance cancellations and/or rate increases were due to discrimination against the properties because they are affordable communities for low to moderate income residents. While the actual data does not specifically identify a national trend in any of the reasons cited for the rate increases or policy cancellations – the question of "why" these cancellations and cost increases have occurred can be answered in part by the number of carriers who have either left the frame construction low-rise markets, or who have limited their exposure as is the case in Florida. There are a number of questions that remain unanswered, but as noted above, a possible factor in many cases may be that the overall size of the premium relative to the risk being underwritten is at its worst ratio for small properties, which may be older, have by nature fewer fire, wind and earthquake resistant features, and who are usually not large enough to partner with the insurance carrier to affirmatively manage risks going forward. The loss claim history reported by the respondents clearly shows an extremely low loss rate, with a majority of respondents only reporting zero or one claims in a five-year period. It is thus fair to assume that there is some other "driver(s)" behind the cancellations and/or premium increases, since they are not necessarily related to specific claims/losses at any of the particular properties.

And finally, NAHMA is extremely concerned with the likely impacts of these insurance cost increases on the operating health and viability of the properties affected. Most of the respondents (71%) reported that they had to absorb the higher insurance costs by cutting other expenses in their operating budget. The net effect is that owners and agents are forced to determine "where to rob Peter to pay Paul" – and the impact on the quality of maintenance and fiscal health of a property cannot be presumed to be good – especially given the hypothesis that the likely communities affected are small, aging family properties.

While some properties report they are able to borrow from residual receipts or reserves to cover the increased insurance costs for a period – many do not have any or adequate funds of this type to make this a viable short-term solution. Even if such funds are available, borrowing from them is not a fiscally preferable solution – rather, it can be considered analogous to an individual needing to borrow from his/her 401K or other retirement fund to meet daily living expenses – such as groceries – today.

The other obvious possible way to address increased insurance costs – through rent increases – is also not currently a viable solution. While the various affordable housing programs have different mechanisms for applying for and/or receiving rent increases – NAHMA maintains that none of the mechanisms provide for timely and sufficient rent increases to offset significant current year operating expense increases.

On a side note, the current situation also seems to point toward an apparently unforeseen but possibly significant flaw in HUD's fair market rent policy changes enacted through the Multifamily Assisted Housing Reform and Affordability Act of 1997 (MAHRA). While tying rent levels to the market is an excellent policy in many ways, it is also perhaps a real disadvantage to affordable housing in certain circumstances, such as the current insurance market. For example, if large market-rate properties are able – through size, volume or other mechanisms – to avoid severe cost increases, such as those in the insurance market, then they are not likely to increase rents in soft markets as aggressively as they otherwise might. When the market-rate property rents are not moving up, the assisted and tax credit properties have no means to increase rents to cover very real and possibly very significant additional costs.

Positive Aspects Identified by Survey Results

Three positive aspects of this issue can be identified from the survey results:

1) A few of the respondents noted that they were experiencing the same insurance cost increases for their conventional properties, which might point toward an overall hard insurance market for all housing, rather than just affordable housing.

It is likely many insurance experts would agree with this premise. The primary reason given is that the principal sources of revenue for insurance companies – premiums, interest income, and income from stock and bond investments – have suffered from significant challenges in the last several years. Major hurricanes, floods, wild fires, and terrorism events; a stock market that until recently has been down some 30% in three years; and the lowest long- and short-term interest rates in 40 years are among these challenges.

2) Some portfolios of affordable housing (in this survey, NAHMA's larger members) report that their property and casualty insurance costs leveled out in 2003.

Insurance experts regularly point out that the market is cyclical, and that it has rotated through periods of high costs and cancellations three times since the early 1970s. It is possible that the market has recently reached the top of the current cycle and has started back down. Based on the survey results, it appears that members who have large premium billings are beginning to see a moderation in cost increases, while smaller owners are not yet seeing it.

3) The respondents report a very low loss/claim rate, demonstrating that affordable housing can be well-run and well-maintained, and is not by nature any higher of a property and casualty insurance risk than market-rate housing.

NAHMA's position

As noted previously, there are key aspects to this issue that are of concern to NAHMA – and should be of concern to all who work to provide and ensure the availability of safe, quality affordable multifamily rental housing. The majority of respondents to NAHMA's survey – predominately representing small, older, family-oriented affordable housing – have faced property and casualty insurance increases of over 40% or more in the past year. Many of these respondents also dealt with cancellation notices. These huge insurance cost increases can only have a negative impact on the owner/agents' ability to maintain a well-run, safe, quality affordable community within a fiscally sound operating budget.

Owners/agents should not have to choose between draconian cuts in other operating expenses, or shortchanging future maintenance by borrowing from reserves, in order to provide for the very basic need of property and casualty insurance.

Unfortunately, solutions – particularly on a national basis – are few, and they are generally either difficult or costly to implement. Group insurance programs can be administratively difficult to pull together, and other options, such as forming risk retention groups or other pool insurance arrangements, or a captive insurance company, can be administratively difficult as well as very expensive. However, NAHMA is aware that some organizations in the affordable housing arena have begun to take steps in these directions.

NAHMA will actively monitor such developments and continue to report to its members on issues of concern and opportunities for addressing their insurance coverage problems. We will also remain vigilant and advocate to any and all appropriate federal agencies regarding our concerns in this area.

Meanwhile, we also encourage members to aggressively pursue alternative insurance policies and carriers on a local, state or regional basis, since insurance is generally a regional product by nature.

Also, we encourage members to follow up on and address any instances in which they believe they have been subject to unfair or discriminatory insurance practices. Members can contact their state insurance commission or department; a list of state contacts is available at the website of the National Association of Insurance Commissioners, at http://www.naic.org/state_contacts/sid_websites.htm. Also, members may contact their local HUD office.

Finally, NAHMA would like to express its gratitude to the NAHMA and AHMA members who responded to this survey. Your time and effort in helping us improve our advocacy efforts are greatly appreciated.

NAHMA Survey on Property and Casualty Insurance Availability
(November 2003)

1) Property location (please provide City and State or if you prefer, just the State)

2) Number of Units

3) Type of Property:
Family
Elderly
Farm/Labor
Other, Please Specify

4) Approximate age of property (years)

5) Property Name (optional)

6) Was a notice of cancellation received before the expiration of your property and casualty insurance policy?

7) If a notice of cancellation was received, how many days notice did you receive?

8) If your policy was cancelled, what was the specific reason given?

9) If you were able to either renew your insurance policy, or were able to find replacement coverage, what increase in premiums did you experience? Annual premiums went from $________ per year to $__________ per year at the most recent renewal date.

10) Despite the increase in premiums, was the amount of insurance coverage reduced, or deductibles increased, to make it more affordable, as well?

11) How do you plan to cover the increased premium expense in your operating budget in the coming year?

12) For this property, estimate the number of losses you reported to your carrier, per year, over the last 5 years (ballpark estimates are ok):
2003
2002
2001
2000
1999

13) Would you be willing to provide supporting evidence to NAHMA? (i.e., copies of the prior and current insurance certificates, premium history reports and loss history reports, for example). If yes, please contact NAHMA directly at (703) 683-8630.