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Covering One's Assets

As reinsurers raise rates, limit treaties, trophy properties in San Francisco, Los Angeles remain most difficult in the state to insure against acts of terrorism

BY JIM EMERSON
Special to the CREJ

It's a myth that you can't get terrorism coverage for your commercial property. But skyrocketing premiums, limited availability and terrorism coverage exclusions are creating insurance headaches for owners of trophy properties in major markets, like Los Angeles and San Francisco.

Insurance costs are soaring because unregulated reinsurance companies, many of which are based offshore in Bermuda, are demanding higher fees to insure the insurance companies against losses. Others have completely stopped negotiating reinsurance "treaties" with primary insurers, which otherwise would spread the risk from terrorism claims.

Meanwhile, the U.S. Congress has failed to agree on a federal terrorism insurance backstop to cap losses the insurance industry would sustain from another act of terrorism.

With less reinsurance available, primary insurance companies are looking to limit their risk exposure for policies on buildings in selected ZIP codes considered high risk, notably, where large numbers of people congregate and for buildings considered as landmarks.

When quotas are filled in those selected markets, insurers avoid writing more policies.

"Since January, when most came up for renewal, reinsurance treaties have been few

and far between, almost nonexistent," said Peter Moraga, spokesperson for the Los Angeles-based trade group **Insurance Information Network of California, Inc.**

Insurance companies presently are not eager to market terrorism insurance as stand-alone coverage, and usually include such coverage only as a convenience and part of a package to close deals with clients, Moraga said.

Stand-alone Policies Rare

Few companies, except for large firms such as **American International Group, Inc., ACE USA, Berkshire Hathaway and Lloyd's of London**, write stand-alone policies for terrorism insurance for California properties. Upward limits on coverage typically range from \$100 million to \$150 million per risk, according to Crittenden's Specialty Coverage Insider, a Novato-based insurance industry newsletter.

Smaller companies such as **Firemen's Fund and CNA California** typically set separate sublimits for terrorism as part of regular property policies, or completely exclude terrorism insurance for larger properties deemed more risky, according to insurance brokers.

Terrorism insurance coverage is available through unregulated policies referred to as "surplus lines" in the insurance industry or through customized "manuscript" policies negotiated between property owners and insurance companies, according to industry



Jenny Jones, President-Elkins/Jones

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Elkins Jones Insurance Agency Inc.

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On regular property policies, most states allow a \$25 million nationwide damage threshold on terrorism claims and a total exclusion on biological and chemical incidents. California Insurance Commissioner Harry W. Low prohibited these industry exclusions on policies offered in California, calling them overly broad and unreasonable.

The state's Department of Insurance prohibits exclusions for terrorism coverage on standard insurance forms, but companies can still legally apply for exclusions on individual lines of insurance offered in California.

"Virtually every major insurance company has filed for terrorism exclusions," said Nanci Kramer, spokeswoman for the state Department of Insurance. "Legally, we cannot deny exclusions, but we can hold their feet to the fire on the wording," Kramer said.

The state examines each exclusion request case-by-case to consider limits and make sure the policy wording doesn't exclude hate crimes, vandalism or malicious mischief, under the broader language pertaining to terrorism, Kramer said.

Lending Liability

According to insurance brokers, insurance problems for property owners typically begin with a letter from their lender demanding proof of terrorism insurance coverage.

In some instances, borrowers who need to refinance properties may be charged extra loan points, if the property owner cannot show proof of terrorism coverage.

While it's becoming more difficult to find terrorism insurance in parts of downtown San Francisco, property owners in greater Los Angeles are experiencing more problems, according to David Haslam, vice president of marketing for the nationwide wholesale insurance brokerage firm **Cargill Sherman & Associates**. His Phoenix-based firm recently arranged terrorism coverage for two apartment complexes in California.

The most difficult places to buy terrorism insurance in California are Beverly Hills, Burbank, Culver City, Inglewood, North Hollywood and Studio City. Yet, the problems property owners have finding terrorism insurance in California pale compared to what Manhattan property owners face in New York, where some insurance companies have actually stopped writing policies in some areas, Haslam said.

Whenever the capacity to write policies gets tight the prices go up. Capacity reflects the

amount of coverage an insurance company can offer and be able to pay claims.

Haslam said this year was no exception as pricing on property insurance increased about 20 percent — not including terrorism insurance — and insurers told their customers that terrorism coverage would now be sold separately.

Most property owners buying terrorism insurance today are forced to get the coverage by mortgage lenders such as **Bank of America, First Union Bank and Wells Fargo Bank**, according to Haslam, who said he knows of about a dozen lenders forcing the issue with borrowers. Others on his list include **Deutsche Bank, Key Bank, La Salle National Bank and Sun Trust Bank**.

In September, Fitch Ratings and Moody's Investors Service downgraded the ratings on commercial mortgage backed securities, backed by pools of mortgages sold to institutional investors, citing concerns about insurance coverage on properties.

According to a recent survey conducted by the **American Mortgage Bankers Association**, the problems with terrorism insurance have led to the delay or cancellation of more than \$15.5 billion in real estate transactions, in 17 states, including California.

The inadequate supply of terrorism insurance has stalled or derailed at least 24 office projects, 10 retail projects, eight apartment projects, six hotels and industrial projects and three mixed-use developments, according to a national survey by the **Real Estate Roundtable**.

Size Matters

Unless the property is large and in a major

market most insurance companies writing policies in California haven't elected to apply terrorism exclusions to policies, according to Jenny Jones, president of **Elkins Jones Insurance Agency, Inc.**, based in Santa Monica.

"They won't write on larger properties in major markets, but I'm sure it wouldn't be a problem to find terrorism insurance in markets like Fresno," Jones said.

A recent survey conducted by the **Building Owners and Managers Association** revealed about one-quarter surveyed were unable to obtain terrorism insurance, and about 80 percent of the 73 percent with coverage incurred higher premiums.

The problem for most property owners is the cost of terrorism insurance, which continues to increase, leaving most property owners unable to afford it, but coverage is available, Jones said.

"We had one client that we quoted \$30,000 for terrorism insurance on an office building in San Francisco, but they didn't take it at the time," she said. "When they came back the quote increased to \$75,000."

The insurance brokerage is presently trying to find terrorism coverage for a \$23 million office building in San Francisco, but so far the cheapest quotes obtained for the client range between \$75,000 and \$150,000, said Jeff Shibata, senior vice president at Elkins Jones.

About eight months ago, Elkins Jones arranged for a terrorism policy on a \$26 million shopping center in Orange County for a \$33,000 premium, but the same coverage today would probably cost about \$50,000, Jones said.

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