



Transforming HOA Insurance: A Call for Proactive Risk Management

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Insurance has become a nightmare for many associations, with heartless insurance companies seemingly poised to undermine the common interest community industry. As an insurance broker specializing in Homeowner Associations (HOAs), I encounter this sentiment daily from board members and community managers. While insurance companies base their pricing on risk factors and past loss history, the real solution to the high cost of insurance might lie outside their rate structures.

Insurance rates are shaped by a multitude of factors, including primary risk rating factors, the age of the building, construction type, reinsurance considerations, and the association's historical loss data. If an association maintains a clean loss history, it typically results in reduced costs; however, a history of past losses can trigger a substantial increase in premiums. Despite the reliance on accurate mathematical models by insurance companies, the fundamental challenge remains rooted in the need for proactive risk management strategies before any losses occur.

Having worked in HOA insurance for three decades, my observation is that a substantial portion (75%) of property losses can be attributed to a lack of preventive maintenance and inspections. In the insurance submission process, we routinely obtain the association's reserve study. Unfortunately, 50% of these studies reveal funding levels are less than 50% of the ideal funding needed. This results in a lack of preventive maintenance. Not adequately funding the reserves can create liability claims related to the board's fiduciary duty in managing the HOA and its assets.

Low funding often results in the extended use of components beyond their useful life, contributing to property losses. When confronted about preventive measures, boards often cite financial constraints, stating that "we cannot afford it." This attitude necessitates a paradigm shift in the industry towards acknowledging that "we cannot afford to let deferred maintenance control us." If homeowners cannot afford their homes due to maintenance issues, perhaps selling and purchasing a more manageable property is a viable option.

Frequently, I witness associations neglecting property maintenance, only to suffer water and sewer claims, causing insurance costs to skyrocket from \$25,000 to \$150,000. The knee-jerk reaction is to increase assessments to cover the insurance cost increase. The real solution lies in a more significant assessment increase to address building system changes needed to avoid future claims. The reluctance to embrace such increases often stems from homeowners' financial concerns. To continue in not repairing the components causing the losses, will only result in additional cost increases. The sooner we address maintenance issues the lower the long-term cost.

To address these challenges, boards should formulate plans to eliminate deferred maintenance over the next few years. This involves funding reserves adequately, replacing components at the end of their useful life, and assessing the real cost of operating the HOA. For associations with low claims history and still in a standard insurance market, maintaining low premiums involves raising the property loss deductible to \$25,000. Each owner needs a comprehensive personal policy which should limit the owner's risk to his policy deductible.

Implementing a deductible policy that clearly defines responsibility for uncovered loss portions and prorating assessments based on damage incurred by each homeowner can ensure fair distribution. It's essential to avoid the futile exercise of assigning fault, as property claims are unrelated to fault and often challenging to determine accurately.

A written maintenance policy advising owners on regular tasks, such as changing washing machine hoses, water heaters, and cleaning dryer vents, can significantly contribute to loss prevention. Regular inspections for uneven surfaces, coupled with prompt fixes. Placing reminders in newsletters and with billing statements. Adding language to vendor contracts indemnifying the HOA from occurrences related to the services being provided. Requiring all vendors to name the HOA as an additional insured. primary coverage with waiver of subrogation. Listing specific tasks that are the vendor's responsibility such as maintaining and repairing sprinkler systems and lighting.

In my extensive experience, well-maintained HOAs with full reserve funding and proactive preventive risk management practices that has addressing issues caused during construction tend to experience lower claims. By addressing these issues, associations can effectively lower costs and foster a more resilient and financially sustainable community.