Insurance Newsletter
Fall 2017

Hurricanes and Insurance Market Trends

Here is the scorecard: Three Class 4 hurricanes struck U.S. territory in the third quarter. Worldwide, there were other tropical storm, flooding and wildfire events, three earthquakes in Mexico, and as this is written large parts of northern California are ablaze (bad news for those who like fine wine), inflicting more economic damage, often in places ill-equipped to deal with it. Taken together, 2017 will potentially rank as one of the worst years ever for natural disaster losses.

So, what are the chances all these events will translate into higher insurance costs? When you read about the amount of damage resulting from these events in general news sources, what they are usually referring to is economic damage, the total dollar impact on people and economic activity from an event. Economic losses from these events are certainly severe, but they don't automatically translate into insurance claims, and its insurance claims that drive insurance costs.

Consider: in order of magnitude of economic damage, of the three hurricanes Harvey in Texas was probably the worst, followed by Maria in Puerto Rico and then Irma, mostly in Florida. But most of Harvey's damage in Texas was flood related; flood losses to property other than motor vehicles are mostly covered, if at all, by the federal flood program, not insurance companies. Much of the damage inflicted by Maria in Puerto Rico was wind related and thus potentially covered by insurance, but many of the storm's victims, especially in poorer areas, did not have insurance. Irma looks like it will turn out to be the most expensive of the three storms from an insurance claim perspective; it was mostly a wind event and thus covered by most insurance policies, and it struck a built up area of southwest Florida, resulting in lots of claims. And of course standard fire insurance will respond to California wildfire losses.

This pattern repeats all over the world, with much of the damage from natural catastrophes either not insured or insurable (flood and earthquake) or occurring in countries or locations where many people just don't carry insurance. Natural catastrophes may make a lot of headlines and affect many people, but each event must be scrutinized individually to understand the actual insurance impact.

Even so, the financial impact on insurance and reinsurance companies from our U.S. hurricanes and wildfires will be sizeable. At the moment there don't really seem to be any two overall loss estimates that are the same, but the numbers all have one thing in common, they are big.

So, what does all this mean to you? Insured losses are spread out throughout the insurance industry, with reinsurers feeling much of the impact. The industry has plenty of capital to handle the losses. Moody's reports that losses from our three U.S. hurricanes alone will likely be an earnings event for most insurers, while causing only modest capital depletion for some reinsurers. Nevertheless, industry news sources are already predicting premium increases in the near term. If this proves to be the case, any increases will likely prove to be small (single digits), and will start to be seen with January renewals. In short, probably not much to be overly concerned about.

There is another important lesson to be drawn from these recent events. Lots of money is needed to recover from them. Absent insurance, government funds are predominantly directed to repairing roads, bridges, power grids and other infrastructure. Any financial aid that reaches individuals or companies comes from government grants and loans, or non-governmental organizations and charities. Funds from these sources tend to be in much smaller amounts, require lots of paperwork, come with strings attached and take a long time to get to where they are needed. For events not covered by insurance, recovery is complicated, and slow.

Insurance companies, on the other hand, are often underappreciated but are nevertheless excellent sources of copious amounts of money,

delivered in large chunks, quickly, and directly to affected individuals and organizations who need the funds the most after an event. Folks impacted by uninsured events fare less well, but where insurance companies are supplying funds, recovery tends to be much quicker and less stressful. When it comes to sources of money to pay for restoration after an event, insurance will always be far and away the best option.

Insurance Basics: Who Is Insured?

One of the most fundamental aspects of any insurance policy is proper identification of who is actually insured. This often isn't as clear as it might seem and mistakes can be costly, so here's a quick walk through some basics.

There are four different types of Insureds, each with different rights and responsibilities under a policy:

The First Named Insured: This is the primary entity or person covered by the policy. The first Named Insured can be thought of as the owner of the policy, with all the rights and responsibilities that go with that. Rights include the ability to add to, delete from, amend or cancel the policy, receive all notices including cancellation or nonrenewal notices, receive any return premiums, and make claims; responsibilities include accurately and honestly completing applications, paying premiums timely, and giving proper notice of claims in accordance with policy conditions. There may often be additional named insureds, but only the one insured can be the first named insured, and have these rights and responsibilities.

Additional Named Insureds: Depending on the policyholder's structure there may be other related, owned or affiliated entities that need to be covered. Additional Named Insureds can be individuals, corporations, limited liability companies (LLC), partnerships, trusts, etc., but there must always be some affiliation or commonality with the first named insured; insurance companies will have their own underwriting guidelines on combinability based on shared ownership or commonality of interests. These will be specifically listed and shown on the policy as additional Named Insureds. They will be covered by the policy to the extent of their interests, but they do not have the same rights and responsibilities as the first Named Insured; their rights consist primarily of the ability to file claims under the policy.

Defined Unnamed Insureds: Policies also typically include otherwise unnamed persons or entities, defined by position or relationship, as insureds other than the Named Insured(s). For example, Section II of the standard Commercial General Liability form is "Who Is Insured", and adds by definition (but not name) spouses, LLC members, officers, employees, real estate managers and others to the policy as Insureds. Don't assume this list will be the same with all policies; there are wide variations between types of insurance and policy forms. While these other defined but unnamed insureds are covered by the policy, like additional named insureds they don't have the same rights and responsibilities as the first Named Insured.

Additional Insureds: The last and lowest tier of insureds, Additional Insureds enjoy few rights on a policy other than the most important one, the right to make a claim for coverage for a loss. However, that coverage can be subject to specific conditions, limitations or exclusions that only apply to additional insureds. Of specific importance, additional insureds usually have no rights to notice of change, cancellation or non-renewal of a policy from the insurance company, even though it is very common to see that requirement.

All this is not as complicated as it might seem at first blush. The first Named Insured applies for, owns and controls the policy, and pays for it. Additional Named Insureds are those other persons or entities that are owned, controlled or affiliated with the First Named Insured and which are covered almost equally in the policy; there must always be some defined relationship with the first named insured for additional named insureds to be added to a policy. Defined unnamed insureds are typically those that would be associated with the insured entity. Additional Insureds are those outside, unaffiliated entities that the named insured has in interest in

including for coverage under the policy, but with limitations not applicable to other classes of insureds.

Common problems here include failure to list every person or entity that needs to be covered. For larger or more complex organizations, that could be a pretty long list, and underwriters will want to understand the relationship of each entity to the first Named Insured. Blanket Named Insured endorsements are sometime available, but must always be used with caution, since they may not extend to all types of entities that may need coverage.

Also often overlooked is the need to add newly acquired or formed entities to policies as Named Insureds; be alert to that need. Another common issue arises when an entity is shut down or divested; there is often a tendency to want to remove that name from a policy right away. Claims can roll in the door long after such an event; best to let those names stay on the policy for a while, perhaps as long as several years, to be sure of coverage. Remember, there is usually no premium charge to add or leave a name on a policy.

Ultimately, insurance policies only respond to protect persons or entities that are listed as Insureds. Getting the Insured correct is the basic first step required to have any potential for coverage to apply, and care must be taken to assure this is done right.

Avoid Problems with Out of State Workers Comp Claims

Here is a fairly common problem that can arise for any employer. As an employer you know you are responsible for providing benefits under your state's workers compensation laws to any of your employees who suffer an on the job injury. Most employers do that by buying a workers compensation insurance policy to fulfill their obligations under the law. Most employers think of their workers compensation policy and their workers compensation coverage as one and the same. Actually, the workers compensation policy is divided into several sections, with Part One being the actual workers compensation coverage.
The Part One coverage agreement under a WC policy is simple and straightforward: to quote,

> *"We will pay promptly when due the benefits required of you by the workers compensation law."*

There is a bit more than that, of course, but the entire Part One insuring agreement for workers compensation runs to only a single page of verbiage. Essentially, the policy doesn't define what it pays; the relevant workers compensation law of the state, or states, does.

The whole Workers Compensation policy is only six pages, probably the shortest insurance contract you'll ever see, and is pretty simple, but it does have one potential pitfall to beware of; it's obviously important to know what state workers compensation law applies. That's established on the policy information page; Item 3.A (for most states and insurance carriers) specifically designates the states where the workers compensation policy is applicable. Each state in which the policyholder has operations must be listed here. Part One coverage does not apply to claims filed under the workers compensation laws of other states.

What about incidental exposure to other state's workers compensation laws? Part Three, Other States Insurance, covers that. With this coverage, workers compensation and employers liability insurance is provided for incidental exposure in states listed here, but not listed in Item 3.A of the Information Page.

So, what happens if you have operations in other states, or for one reason or another have employees who may be hired in or work in other states? Does your policy respond, and how? Imagine a not uncommon situation where an employer hires a sales person or service technician in another state to service customers in that area. For Part One coverage to apply, those states must be specifically listed on the policy in item 3.A, at the inception of the policy. That's because Part Three, Other States Insurance, has a catch; It says two things:

> *"If you begin work in any … states after the effective date of this policy … all provisions of the policy will apply as though that state were listed in Item 3.A. of the Information Page.".*

That's good, but it adds:

> *"If you have work on the effective date of this policy in any state not listed in Item 3.A…coverage will not be afforded for that state unless we are notified within thirty days.".*

Translation: if you add a state, it's covered automatically under Part Three, but *only* until that policy expires. At the next renewal, you must list that state in order for coverage to continue.

The other thing to understand is that the workers compensation statutes of most states will have extraterritorial provisions that specify when and how their workers compensation act applies, both in and out of state. Normally, the state statute will indicate that if the principal place of employment is within their jurisdictional boundaries, a workers compensation injury occurring outside of state boundaries is still covered by the state law; if the contract to hire was negotiated within their state, their workers compensation laws apply regardless where the injury occurs. Additionally, workers compensation statutes also normally specify that any work related injury occurring within their borders is subject to their workers compensation statutes, even for employers and employees whose place of business is not within their state line boundaries.

So think about that. When an employee is injured in another state where the employer does not normally do business, the extraterritorial provisions of the state workers compensation act work great, as long as the employee elects to utilize the benefits of the home state workers compensation act. The problems occur when the employee elects to file the claim in a state where the employer does not have a physical location and the employer does not have workers compensation coverage.

The usual reason an employee files for benefits in a state other than the home state is the amount of disability benefits that will be paid. Consider a highly successful salesman from State A, earning $2,000 per week. Workers compensation disability benefits are generally calculated at 2/3 of wages, up to a maximum set by each state by statute. State A caps weekly disability benefits at $600 a week, so that's all this employee would receive if he filed a claim for a work injury under State A law. Suppose he was injured while visiting a client in State B, which has a high maximum weekly disability rate; under that state's law he will receive $1,333 per week while unable to work. Most employees would not have a problem figuring out what to do in this situation.

This creates a coverage issue for the employer, albeit one that easily fixed. When the workers compensation policy is purchased, the employer should be sure it specifies in Item 3. A. all states in which the employer has a physical presence, even if only a single salesman. The Other States provision is item 3.C of the Information Page. Here is where you list other states where there may be incidental exposure. The best way to handle that is to insert the following omnibus wording in Item 3.C: "All states and US territories except North Dakota, Ohio, Washington, Wyoming, Puerto Rico and the U.S. Virgin Islands (these are the four monopolistic states and two monopolistic territories where the state/territorial governments provide workers compensation coverage) and those states listed in Item 3.A.

This blanket "all states" wording eliminates the possibility of accidental oversight where a state is left out and no coverage would therefore be available. Even with this, though, there will always be an unavoidable potential risk created by the monopolistic states and territories, North Dakota, Ohio, Washington, Wyoming, Puerto Rico and the U.S. Virgin Islands. If you come anywhere near those jurisdictions, talk to us about custom solutions.