

Strata Insurance Changes – 2013

By Shawn Fehr, Seafirst Insurance Brokers Ltd.

Since the beginning of 2013, Strata Insurance premiums began to rise on Vancouver Island. A significant cause of the increased rates is directly attributable to Earthquake Insurance. I have summarized some of the reasons for this below:

Updated Computer Modeling

When a disaster occurs anywhere in the world, the loss is analyzed from an insurance perspective. RMS (Risk Modeling Solutions) is a company that gathers data and provides information to organizations that work within the Insurance Industry. For example, when earthquakes occurred in Chile, Japan and New Zealand, RMS was able to obtain data and update their computer models to provide a more accurate assessment of what we could expect from a large earthquake on Vancouver Island.

Government Regulators

OSFI is the Office of the Superintendent of Financial Institutions. Among other things, they oversee the sale of insurance in Canada. After OSFI received the updated data from RMS, they amended their regulations to require that Insurers increase the capital reserves they must keep on hand to pay out potential losses that could occur.

Insurance Company Options

The amendment of the OSFI regulations essentially gave Insurance Companies two options: they could purchase more Reinsurance to cover the Earthquake accumulations that they have on Vancouver Island or they could reduce their Earthquake accumulations to a point where their existing reserves were adequate to cover what they had in their portfolios. Both of these options have led to increased premiums.

Option 1 – Purchase more Reinsurance

If the Insurance Company purchases more reinsurance to cover the cost of Earthquake, then they usually will pass that additional cost directly to the policyholder. The high demand for Earthquake Reinsurance forces an increase to the cost of this coverage in the first place. The end result is a higher reinsurance cost that is passed directly to the policy holder.

Option 2 – Decrease Earthquake Accumulations

There are Insurance Companies that are reducing their Earthquake accumulations on Vancouver Island. Specific postal codes (V8R, V8S, V8V) have been targeted as areas of higher exposure and some Insurers have elected to reduce their highest exposure accumulations by not writing business in these areas. Other Insurers are still willing to write insurance in these areas but will not offer Earthquake coverage. When one Insurer exits the marketplace it leaves a void that other Insurers are forced to fill. The result is that those markets must charge higher rates, for

the reasons outlined in Option 1 above. The laws of supply and demand also have a significant impact at this level as the demand for Earthquake is very high but fewer Companies are able to provide the coverage.

Deductibles

Another method that Insurance Companies are using to control their Earthquake exposure is to use higher deductibles. A few months ago, a standard Earthquake deductible in most scenarios was 10% but is now increasing to 15% or 20%. An increase in deductible means that the amount that must be paid out by the Insurer after a loss is reduced and, therefore, the money they must keep in reserve is reduced. It is important that all Strata Owners understand the amount of Earthquake deductible that could be assessed in the event of a loss and be sure that they have a high enough Loss Assessment limit on their Personal Unit Owner's policies to cover this. For example, a \$10,000,000 building with a 15% Earthquake deductible has a deductible of \$1,500,000. If there are 50 owners in that building, and it is destroyed, then each owner will be assessed their share. For the sake of the example, let's say each owner's share is equal – the share is \$30,000 per owner. (Of course, the actual amount would be calculated on the basis of unit entitlement, thus an owner's share could be much higher than this average of \$30,000.) This could be a significant amount of money to come up with if it is not properly insured – especially at a time of trauma following a devastating Earthquake.

Local Rating

For many years, Victoria has enjoyed below-market Strata rating. We have essentially flown under the radar. In spite of the fact that we live on an island that sits very near a significant fault line, we have enjoyed relatively low strata insurance rates when compared to Vancouver and other neighbouring Insurance markets like Seattle. Many Insurance Companies participated on Strata programs in Victoria and, based on large volumes, were able to maintain lower than market rating. With the changes required by OSFI, it no longer makes economic sense for them to continue on programs that demand low rates.

It is an interesting situation that arises when Earthquake Aggregate is in high demand and the Reinsurance Company looks at their options of where to sell their Earthquake coverage. If they sell it in Victoria than they can obtain a certain rate but if they sell it in Vancouver they could probably get twice the Victoria rate. Economically speaking, it makes much more sense to provide the coverage where they can get the most profit.

The Future

Presently, in Victoria we are involved in a "transitional market" while Earthquake rating gets sorted out. Strata Corporations in Victoria and on Vancouver Island should prepare to see increases in insurance rates. As noted above, the rates in Victoria are still well below the Vancouver rates, yet it could be argued that the earthquake exposure is greater on Vancouver Island than in the Lower Mainland. Given the latest data collection and computer modeling it is apparent that Victoria is now firmly entrenched on the radar – we can no longer hide.