Texas Council Risk Management Fund

BULLETIN

Covering Community Centers since 1988

How does the Fund Provide Property Coverage?

Texas community centers participate in the Texas Council Risk Management Fund to protect their most important assets. A Fund member covers their employees for injuries on the job through workers' compensation. Their vehicles and equipment are protected if they cause injury or property damage to members of the public and the center is protected if its operations, premises or facilities cause harm to others. The district's board of trustees, officers and employees are protected against allegations that their decisions or actions have caused harm. Licensed professionals are also protected if there are allegations that the delivery of professional services caused harm or injury to their clients. Center owned property, including buildings, office contents, furnishings, computers and software, equipment and vehicles are also protected against loss. The following description of property coverage is provided for general knowledge and does not replace, amend or alter the language in the Fund's Property Coverage Document.

The Fund provides very broad property coverage for members' property. The insuring agreement in the coverage document grants the coverage based on the idea that if something is not specifically excluded or insured by some other type of coverage, then the property listed on the policy is covered. The actual agreement says:

> ***INSURING AGREEMENT***
> ***This agreement covers scheduled property, as described in this agreement, against all risks of physical loss or damage, except as hereinafter excluded, while located as described in this agreement.***

The property owned by the Member can include buildings, office and shop contents, mobile equipment like mowers and other miscellaneous equipment such as tools, woodworking equipment, signs, fences and security gates. If a property is not owned by the member but a contract or lease agreement requires the member to cover it, that property can be included for coverage. This is a typical situation for leased equipment like office copiers or computer equipment.

The type, location and value of the property must be listed in the schedules attached to the coverage document for the Fund to provide coverage. Here are examples of the major types of property and how they are described in the schedules with actual examples from member property schedules:

- Building – by its address, occupancy, square footage, type of construction and value:

    2626 S. Clack St, Outpatient Clinic, 22,552 square feet, Frame*, No (in Flood zone) $2,180,270 (building value)
    Abilene, Taylor 79606-1557 (city and county), 1980 (year built) NNS (territory designation for wind and hail) Replacement Cost (basis of coverage)

    **Frame is a rating class for buildings that are constructed of wood framing with siding or brick veneer*

- Contents – same descriptive terms as a building and the contents' value at that location,

    $477,396 (contents value at above address)

- Boiler and Machinery – description of equipment, location, serial number (if available) and value

    Weil-McLain, 88 Boiler, MDL #P (133) 2519 Scripture St, Denton, $31,827

- Electronic Data processing Equipment – make, model and type of component, location, serial number and value

    58 1948 AVAYA PHONE SYSTEM (70) 2616 S Clack St, Abilene $131,472

- Mobile Equipment – description, serial number, value,
    Kubota Tractor zero turn zb326s w/mower deck, 75402 $16,000 ACV
    Mitsubishi Forklift $10,891 ACV

- Miscellaneous Property – description, location, serial number if any, value
    14' Security Gate, 744 Hickory, Abilene $11,595

In addition to the listed property, there are extensions of coverage that provide automatic and additional amounts of coverage. The Property Coverage Contribution Worksheet that is included with each coverage document lists some of the important provisions about valuation, deductibles and ancillary coverages like Flood and Windstorm. One of these "automatic provisions" is very important for protecting each member fully. The Worksheet includes the "Blanket Limit Each Occurrence" provision that serves as a failsafe for individual properties that may not be valued sufficiently to meet the replacement cost. This provision states simply that in the event of a claim the <u>total</u> insured value is available to pay for the loss. In the example of covered properties illustrated above, the building is valued at $2,180,270. The total value of all insured property on the coverage document is $20,597,933. In the event that the building is totally destroyed and the actual cost to replace the building is $3,500,000, it would be covered because the total limit of over $20 million is available to pay the full amount of the loss. Effective coverage for the member still depends on proper valuation of properties, but the Blanket Value provision protects the member if something is overlooked, there are mistakes in the valuation process or construction costs are rising more rapidly than the annual re-valuation process can keep up with.

There are three forms of property valuation, replacement cost, actual cash value and agreed value. Replacement cost is generally defined as the current cost to replace a property with something of similar kind and quality. Each year about 20% of members benefit from a professional, physical appraisal of their property. The rest are subject to revaluation based on a formula that updates property values using national construction cost factors modified by zip code factors to provide a "best estimate" of what it would cost to replace. The other common method of valuation is "actual cash value" which represents the depreciated value of property at a particular time. This is the basis of value of mobile equipment like forklifts and mowers. In most cases, the actual cash value is less than replacement cost. In rare cases an "agreed amount" may be assigned to property that is unique, rare or for which there is difficulty in determining an actual or replacement cost basis.

The coverage for all of the classes of property described above is for "***all risks of physical loss or damage, except as hereinafter excluded.***" The next question then is "what are the exclusions?" The enumeration of exclusions is a tedious process but it may help to think of them in several broad categories. One major category of exclusions in all property policies is for manmade events that are essentially uninsurable because of their widespread and catastrophic nature. Nuclear contamination, war and "hostile or warlike action in time of peace," insurrection or rebellion, terrorism and detonation of a nuclear device are actions that are excluded or for which there is only limited coverage. Other "manmade" acts that are excluded are "dishonest or fraudulent acts committed by the member's officials, employees, volunteers or agents." (Crime coverage or public official's bonds may respond to criminal or illegal actions by these people.)

Neglect in maintenance, wear and tear, rust, corrosion and faulty workmanship are also excluded. Damage caused by insects, animals or vermin is excluded. Loss of use and the cost of remediation due to fungal pathogens, asbestos, fungus, mold or mildew are excluded. A common element of these exclusions relates to the process of maintaining a structure so that it is clean, in good repair and subject to efforts that help prevent damage or deterioration. In other words, the coverage assumes that the member will take good care of their property.

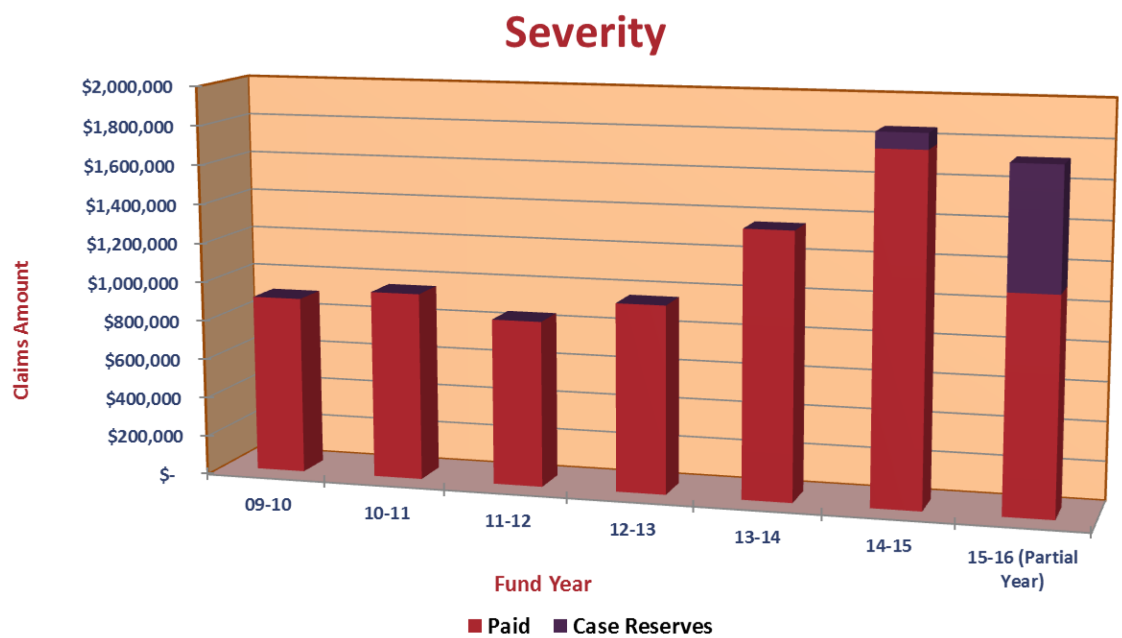
Natural events that are not covered include flooding in a "high hazard flood zone" as determined by FEMA's National Flood Insurance Program. This is generally flood zone A or within the designated area of a 100 year flood plain or storm surge zone. Flood damage occurring outside of zone A is covered by the Fund up to $10,000,000 per occurrence. Other natural occurrences such as changes in temperature or humidity are excluded from property coverage. The incursion of rain, sleet, hail, snow, sand or dust into a building is excluded unless the building first sustains damage to its roof or walls that allows it into the building.

The loss of incoming utilities such as electricity, water, gas, steam, refrigerant or outgoing sewage caused by events away from the covered premises are generally not covered, either. The concept of utility also includes "incoming or outgoing voice, data or video." These exclusions take effect when the event that causes an outage occurs away from the covered property. An example of this would be a lightning strike at a power substation a mile away that interrupted electrical service to the member's administrative offices. A lightning strike to the administrative offices would be covered but not any damage that occurred because of a distant power outage.

There are other exclusions to the effect of laws or ordinances, and "faulty, inadequate or defective" planning, zoning, design, surveying, construction, maintenance, remodeling, materials and other activities related to building processes. So, the grant of coverage in the insuring agreement is broad and the list of exclusions seems extensive. But the exclusions focus mainly on events that are intentional in some way, the result of neglect, actions by government or don't directly affect the buildings or contents covered. What is covered is quite broad and the next section lists some of the common kinds of claims covered by the Fund to illustrate the breadth of coverage.

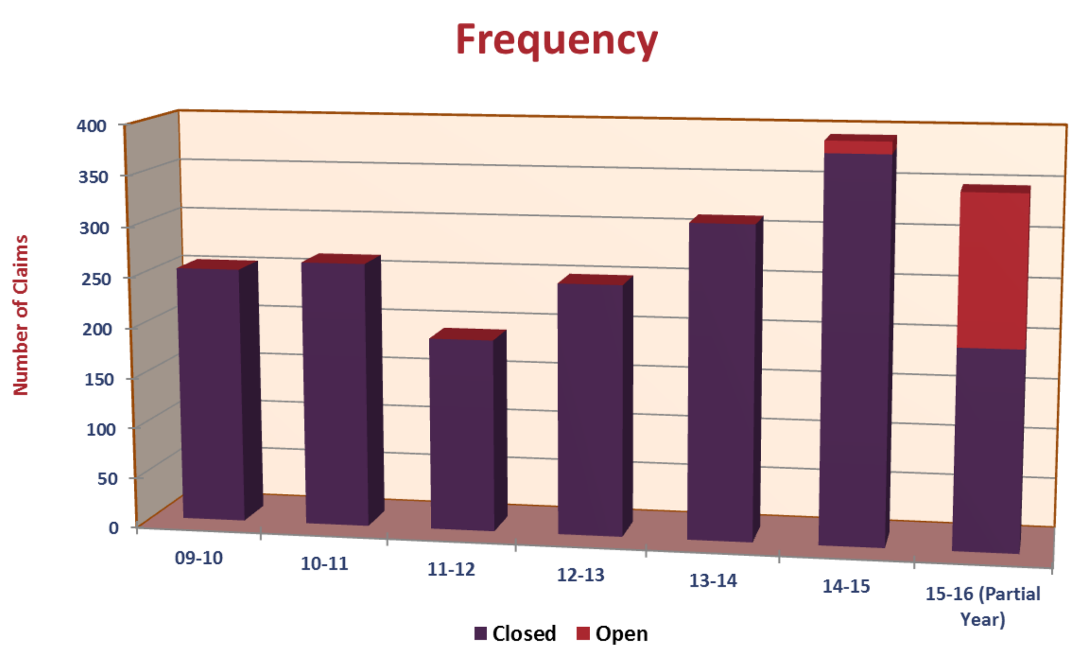
In the spring of 2016 many parts of Texas were pummeled by hail storms. As of October 1, 2016 the Fund had paid or reserved over $1 million to pay for damage to roofs, windows, siding, cars, pick-ups, vans, awnings and signs. Other types of recent weather related claims to buildings, contents and building equipment included lightning strikes to servers, phone systems and air conditioning compressors, wind damage, freezing of water pipes, ice storm damage to gutters, vents and roof and flood damage (not in Flood Zone A). Other types of claims included vandalism, theft of mowers, weedeaters, rooftop air conditioning units and laptops. A dog in a client's home spilled a drink on a case manager's laptop, a toilet overflowed and a large pine tree fell on a group home. Since 2004, claims were also paid because of Hurricanes Ike, Rita, Dolly and Claudette.

The following chart illustrates the amounts of claims paid by the Fund for damage to members' property since 2010 as of June 30, 2016.



The variability in the chart reflects the nature of Texas weather in addition to the activities of thieves, dogs and faulty plumbing.

The next chart illustrates the frequency of property claims for the same period.



As mentioned in the first section of this report there is a provision in the coverage that extends the blanket limit of liability to each and every item of property that the member schedules with the Fund. The only exception would be for items covered on an "agreed amount" basis. That is only one of many extensions of coverage that help protect members of the Fund. The following discussion will explain and list these extensions of coverage found both in the coverage document and the declarations. In some instances the extensions of coverage begin to whittle away at the exclusions. In others, they are outright expansions of coverage that remove ambiguity or add limits of liability.

One of the most important extensions of coverage is automatic coverage for newly acquired property up to $1,500,000 in value for a period of 90 days. This coverage comes into play when someone forgets to notify someone, usually the Fund about a newly built or purchased building. But, the failure to notify can be internal to the member as well when the staff members involved in an acquisition or construction project forget to tell the person responsible to report changes to the Fund. The Fund will add the property to the schedule back to the date the property was acquired or put into service by the member. The Fund will also cover damage to the unreported property as long as it occurs within the first 90 days after center ownership was acquired and does not exceed $1,500,000.

Extensions of coverage also come into play in the aftermath of damage to member property that results in claims to the Fund. After many serious claims that result in heavy damage to buildings and facilities there is a significant clean-up cost before repairs or re-construction can start. The coverage document affords up to $500,000 for debris removal. An additional extension provides up to $500,000 for demolition costs. Another significant aspect of rebuilding – the increased cost to conform to new building codes that were not in place when a building was first constructed is also covered up to $1,000,000. An example of this is the change in building codes that occurred after the devastation from Hurricane Andrew in 1992. Significant changes were made in requirements for strengthening roof structures and securing them to the walls of buildings and houses. Although these changes are not that expensive they do add to the cost of rebuilding a structure that was originally built before 1992. Texas adopted new building codes in 2003 and 2006.

Property in the course of construction is also covered with an automatic $1,000,000 limit of liability. The value of the repairs to a building after a claim is also covered by this provision. This is also known as Builder's Risk coverage and is often provided by the contractor doing the work.

Another part of the coverage afforded members is for loss brought about by an interruption of the member's business. After Hurricane Ike, several members were significantly affected by the storm. One member was essentially out of business for a short time and unable to derive income from the services to its clients at several of its facilities near the Gulf coast. "Loss of Revenue/Business Interruption" coverage will reimburse a member for lost revenue up to $1,000,000 that can be reasonably documented during a period of business interruption. The loss is adjusted by deducting expenses that do not continue during the period of interruption. If a mental health facility is closed by storm damage and clients cannot be seen during the period of restoration, the loss of revenue would be covered by the "Business Interruption" coverage provided in the coverage document. If the mental health facility can resume operations in a vacant storefront at a nearby shopping center, the cost of rent and utilities paid by the member to resume services more quickly would also be covered up to $1,000,000. The process of determining the extent of loss is based on historical records, the costs that do not continue during the period of interruption and fixed ongoing expenses that do continue.

The following list of extensions of coverages is also included in the Property Coverage Contribution Worksheet that is part of each member's coverage document:

Coverage for	Limit of Liability
Fine Arts	as scheduled
Leasehold Interest	$500,000
Personal Effects	$10,000
Vacant Buildings	as scheduled
Trees and Shrubs	as scheduled
Property of Others	as scheduled
Property off premises	as scheduled
Valuable Papers	$250,000
EDP – Media/Software	$250,000
Loss of Revenue/Business Interruption	$1,000,000
Extra Expense	$1,000,000
Loss of Rents	$500,000
Accounts Receivables	$50,000
Flood-Zone A/ No designation	NO COVERAGE
Flood - Other than in Zone A above	$10,000,000
Automatic Coverage	$1,500,000
Property in the Course of Construction	$1,000,000
Expediting Expense	$100,000
Property in Transit	$500,000
Increased Cost of Construction	$1,000,000
Demolition Cost	$500,000
Debris Removal	$500,000
Hazardous Materials Cleanup	$100,000
Rented Mobile Equipment	as scheduled

The list of extensions to coverage represents the Fund's commitment to providing the broadest possible coverage for members. A more detailed description of the various extensions is available from the MGA Team that underwrites and services members' coverages. Many of the terms are also defined in the "Definitions" section of the coverage document.

One of the key principles of self-insurance is risk sharing. The Fund shares risk with its members through the structure of the Fund and the fact that member equity in the Fund is at risk in the event of catastrophic losses that exceed the very high levels of reinsurance protection in place. The Fund purchases reinsurance from insurance companies that specialize in this coverage. A reinsurance program is structured in layers. The first layer is the Fund's retention when the Fund pays the entire claim amount that falls within the layer. Currently the retention is the first $150,000 of any property claim. Above $150,000 a reinsurance company picks up all claim costs up to $600,000. Above a claim for that amount, another reinsurance company provides coverage up to $350,000,000. Beyond that amount, the Fund's assets would be at risk including the member's portion of the Fund's surplus.

Another type of risk sharing is a deductible that must be borne by the member before losses are paid by the Fund. In general, the standard deductible for a property loss ranges from $1,000 to $25,000 for losses to buildings, office contents, computer equipment and any other scheduled property. A member with a $1,000 deductible would have that amount withheld from a $25,000 claim for a roof damaged by hail. In the determination of contributions paid for property coverage there is a credit applied to the rates based on the size of the deductible. The larger the deductible, the larger the discount so that at the higher levels the first deductible might be offset by the credit applied to the rates. The Fund is implementing a separate wind and hail deductible that is now required by the reinsurance companies. The new deductibles for wind and hail are 1% of building value subject to a maximum deductible of $25,000 per building and $50,000 maximum aggregate per occurrence. The aggregate is the maximum amount of deductible that would apply regardless of the number of buildings damaged in a storm.

This description of the property coverage provided to Fund members is not meant to replace any of the terms, conditions, definitions, extensions or limitations contained in the coverage document. The intent is to provide a general understanding of what is and is not covered. Any determination of coverage for a claim is based on the presence of the property as scheduled and the actual language of the coverage in relation to the circumstances of the claim. This determination can only be made by Fund claims adjusters working with the member whose property has been damaged or impaired.