Earthquake Insurance – is your policy on stable ground?

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The recent magnitude 5.4 quake in Southern California may have been moderate in severity and caused minimal damage, but it certainly rattled our memory that we too live in a seismically active area. Most of us remember exactly where we were when the Nisqually quake hit. Personally, I remember rocking and rolling on the 23rd floor of a downtown Seattle high-rise and rushing to pick up my 3 year old son from daycare who upon my arrival happily asked me…..why was the ground dancing? But do we remember how our earthquake insurance was structured and if/how it responded to our magnitude 6.8 event back in late February of 2001? Do we know if our current policy(ies) will stand up tall should another event hit our region?

Protecting human life and health should be the primary focus of how all of us prepare and respond to any potentially disastrous event. However, as prudent business people, we should also be cognizant of protecting the financial health, survival and ongoing success of our respective companies. So what are some of the major things to look for in earthquake coverage?

Earthquake vs. Earth Movement vs. DIC

Insurance contracts can vary widely in how "earthquake" or "earth movement" is defined. Coverage can include/exclude things such as mudslide, mudflow, landslide, sinkhole and volcanic action. Difference in Conditions (or DIC) can provide earthquake or earth movement and typically flood cover too. Flood definitions are all over the map as well and can include/exclude such things as surface water run-off and backup of sewers or drains. Be sure you understand and your broker has negotiated appropriate coverage definition(s) based on your specific exposure, risk appetite and coverage already granted under the "standard" property form.

Deductible Language

Earthquake deductibles can vary widely in both structure and application. Most deductibles for coverage in what's deemed an "earthquake zone" are based on a percentage of the value of the assets insured subject to a minimum flat amount (usually $50,000 or $100,000). Deductibles may be a percentage of total values at risk, total values subject to loss, total values per location, insured values per coverage per location or some other seemingly cryptic wording. Make certain you know how your deductible will be calculated - in detail, based on your current building, contents and business interruption values. We note that current soft market conditions have afforded some lucky policyholders the benefit of a flat dollar deductible of $50,000 or $100,000 (i.e. no percentage applied).

Coverage Extensions

OK, so we now know to pay attention to the basics - primary coverage definition and deductible application. So what else should we take our magnifying glass to? The simple answer is the entire insurance contract, but for those of us that are not sleep deprived, here are a few highlights:

Building Ordinance & Law – policies may stipulate the insurer will not pay for loss caused by the enforcement of any ordinance or law requiring reconstruction or repairs to adhere to previously grandfathered code or requiring the demolition of a partially damaged building. Earthquake codes are often updated as a result of a significant event and, as such, can apply to both old and new construction. Ordinance and law coverage is often available subject to a sub-limit.

Contingent Business Interruption, Off-premises Utilities and Ingress/Egress – policies can neglect to provide coverage for down-time resulting from off-site damage to non-owned property. For example, suppose your building survived the quake with minimal damage but no electricity is available due to significant damage to a major transformer or switch station a mile away. What if customers can't physically get to your hotel due to impaired infrastructure? Or, will coverage apply if your sole supplier can't manufacture and/or deliver a core product component and you have no choice but to shut down operations? Coverage for each of these scenarios may be available through an appropriately negotiated policy.

Extended Period of Indemnity – your insurance contract may limit your business interruption (including rental income) to the standard period of indemnity starting with date of the initial damage up to the time your facility is restored back to like physical condition prior to loss. Let’s say you own several apartment buildings at 95% occupancy which suffer enough damage to make them partially (or is it completely – remember Building Ordinance above?) untenantable. After 5 months of diligent repair, you re-secure your certificate of occupancy but lease-up takes another 5 months. Will the insurance company pay for the additional loss of “market-share” rents post certificate of occupancy? Probably no surprise, but an extended period of indemnity may be available – typically in 30 day intervals (30, 90, 180, etc.) and often at some additional premium.

These are just a few of the “cracks” that may surface in your earthquake insurance policy upon diligent review by an experienced insurance professional. Like most insurances, careful review and negotiation of the contract language can make a huge difference in how your insurance may or may not be respond in the event of a claim. Of course, price is no doubt a consideration, but most underwriters respect the efforts of a knowledgeable broker/agent, ultimately offering acceptable terms and conditions at a competitive price.

If you have any questions or would like to discuss please call us on 425.709.3600.