# Building Blocks

JLT's Real Estate Insurance Magazine

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# Public Liability Insurance, How Much is Enough?

Property owners often ask what limit of Public Liability insurance should they purchase in order to protect themselves adequately against their legal liabilities. JLT would always advise its clients to buy as much as they can afford - but what are the exposures?

## Losses that lead to liability claims?

Generally a liability policy is intended to indemnify the insured for all sums they are held legally liable to pay third parties following personal injury or property damage and consequential business interruption subject to the terms and conditions of the policy. Losses that can lead to the legal liability can be wide and varied but examples of such losses are as follows:

**General property owner's liability losses:**

- Bodily injury to members of the public in and around the premises
- Damage and bodily injury resulting from poor maintenance (e.g. collapse of building, fire, machinery, faulty sprinklers)
- Failure to implement appropriate controls over contractors (e.g. hot works)
- Spread of fire throughout the property and neighbouring properties leading to bodily injury and property damage

**Specific to commercial offices:**

- Damage to utilities leading to interrupted business (especially business where minor interruptions lead to high losses – such as trading exchanges)
- Water damage to tenant's property and consequent interrupted business
- Failure to manage contractors resulting in third party property damage, consequent business interruption and bodily injury
- "Slip and trip" exposures in common areas
- Denial of access to the premises
- Items falling from the building, for example whilst cleaning, injuring members of the public

**Specific to industrial buildings:**

- Building not fit for purpose leading to tenant property damage (e.g. stock) and consequential business interruption
- Non-compliant materials leading to bodily injury, property damage (such as Chinese Fibre Board) and consequential business interruption
- Contamination of tenant's stock
- Damage to utilities leading to damaged stock.

**Specific to retail buildings:**

- High footfall which generates increased exposure to bodily injury arising from exposures such as "slip and trip"
- Third party property damage and consequential business interruption arising from contractors
- Third party property damage and consequential business interruption arising from denial of access
- Damage to items under Care, Custody and Control

## What are the costs?

The cost of legal liabilities resulting from bodily injury incidents can be high. Insurers in Australia have experience of costly Paraplegic claims up to $5m and Quadriplegic claims up to $10m. The legal liability for death will vary depending on the age and specifics of the deceased, such as anticipated earnings, but can be up to $5m.

Depending on the loss and the specialists involved, the legal costs associated with these bodily injury claims can range between $10,000 and $500,000. The legal costs associated with property damage claims are generally lower due to the shorter nature of the settlement of claims.

For third party property damage, the costs will depend on the surrounding assets such as tenants' contents or buildings. If a surrounding building were to be destroyed the reinstatement value of that building could be significant. Whilst there should be insurance in place the third party insurers will look to subrogate against the offending party. Depending on the type of the contiguous property this could be significant (multi-storey property in a CBD location could be in excess of $200m).

Financial loss caused as a result of the interruption to tenants or surrounding businesses through property damage should also be considered as the cost of interruption to some businesses can be high. Again, third party insurers will look to subrogate against the offending party, for example, trading floors (in excess of $100's of millions).

## What are other commercial landlords purchasing?

From JLT's experience with existing Real Estate clients, no single landlord purchases a limit of liability of less than $50m where the reinstatement value is in excess of $100m. Obviously this does not take into consideration the number of assets, the occupation, the location and whether or not the properties are industrial, commercial or retail.

Following discussions with some of the top liability insurers in Australia it is clear that few owners of high rise commercial properties carry a limit of liability of less than $50m (each and every occurrence).

## What about the tenants?

The liability insurances arranged by the landlords do not extend to cover the liabilities of the tenants. The exposure for tenants could, in fact, be higher in commercial offices than for the property owners as they provide an environment that the tenants are responsible for maintaining.

The tenants also operate their businesses within these premises and this generates additional liabilities, depending on the nature of the operations being conducted at the premises.

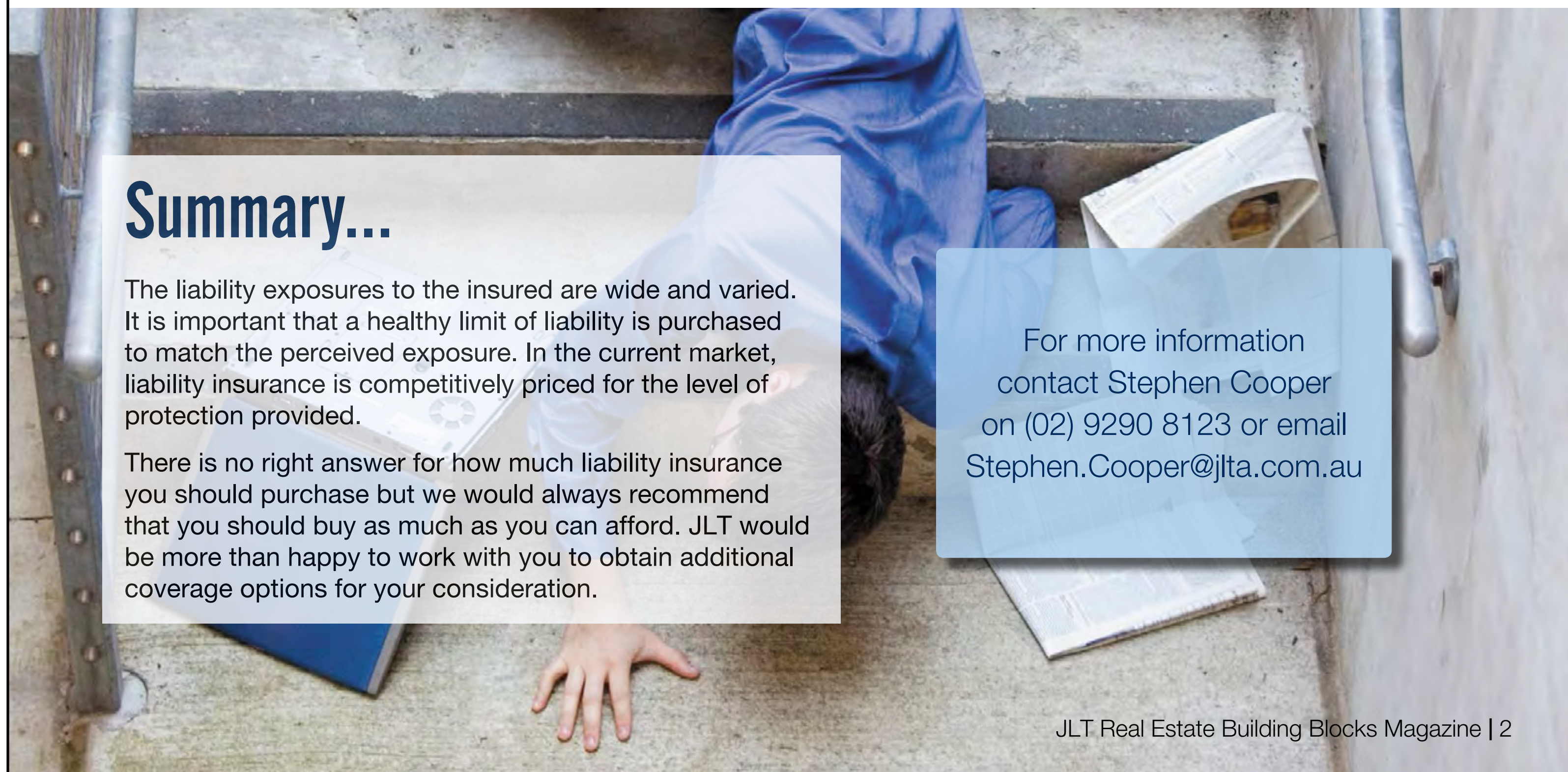
**Tenant's exposures:**

- Damage to the building (high rises are generally in excess of $200m)
- Damage to contiguous buildings
- Damage to landlord's fixtures and fittings
- Damage to property and consequent business interruption to neighbouring tenants
- Bodily injury to tenants and/or the public

## Live examples?

The following claims have been experienced in Australia and though both are yet to be finalised they are already significant in value:

- $40m property damage and bodily injury claims following landslide, where the landlord had altered the environment
- $1bn (estimated) property damage and bodily injury following the spread of fire where the landlord's tenants may have caused the fire



## Summary...

The liability exposures to the insured are wide and varied. It is important that a healthy limit of liability is purchased to match the perceived exposure. In the current market, liability insurance is competitively priced for the level of protection provided.

There is no right answer for how much liability insurance you should purchase but we would always recommend that you should buy as much as you can afford. JLT would be more than happy to work with you to obtain additional coverage options for your consideration.

For more information contact Stephen Cooper on (02) 9290 8123 or email Stephen.Cooper@jlta.com.au

# Psychological Injury in the Workplace

Psychological injury in the workplace is a complex issue for employers which can affect a business's performance. Over the last decade, through a range of public mental health initiatives, there has been a marked increase in awareness about the issue of depression, early identification in the workplace and good practice workplace and clinical management strategies.

**Increasing prevalence of Group Salary Continuance claims payments that are related to mental illness conditions:**

2006 - 10% of all claims.
2008 - 15% of all claims.
2011 - 17% of all claims.

* OnePath statistics

## Psychological Injury in Australia

There is an increased risk that individuals suffering from psychological illness or injury will become entangled in complicated performance and attendance management programmes and conflicts, as well as an increased prospect of workers compensation and salary continuance claims.

At JLT we know that many businesses struggle with this. We have invested in professionals who are experts in this field who can provide you with the support needed to manage complex claims. We work with you to effectively manage everything from pre-injury health and wellbeing initiatives through to claims and injury management and premium reduction for workers' compensation and salary continuance insurance policies.

Real Estate companies typically have streamlined work forces with lower employee numbers than other industries, making each person key to how the business operates. This can mean greater impact on the business is felt by property owners if even one employee is suffering and unable to work.

## What can be done?

As with physical injuries, early intervention is crucial in driving positive outcomes for work-related psychological injuries and illnesses. Alternative psychological early intervention protocols are becoming increasingly utilised, which emphasise the role of:

- The provision of immediate practical support
- Utilisation of effective support networks
- Morale maintenance initiatives (such as key leaders demonstrating organisational support)
- Monitoring of high risk individuals
- Access to specialist mental health treatment (particularly trauma-focused cognitive behaviour therapy) for high risk individual employees



## 5 Ways to Reduce Psychological Injury

There are a number of factors which can affect rehabilitation of psychological injuries and illnesses in the occupational environment. JLT's Benefit Solutions team employs psychologists to work alongside our claims managers allowing us to understand the key drivers in managing the complex nature of these claims. We look to reduce the impact of work-related psychological injury on the business by the following means:

### 1 Establish proactive health and wellbeing initiatives

Proactive identification, monitoring and management of employees experiencing mental health problems reduces the likelihood of these employees lodging workers' compensation or salary continuance claims.

### 2 Encourage a supportive return to the workplace

Clinical service providers who view return to work as the primary treatment focus work collaboratively with insurers and communicate regularly with employers to improve return to work outcomes. This can reduce workers compensation costs by up to 50 percent.

### 3 Ensure efficient claims administration

Delays in claim liability determination can foster uncertainty and distress. Once claims are finally determined, factors related to perceived inequity and unfair treatment can contribute towards entrenching work disability.

### 4 Identify barriers to a safe, timely and durable return to the workplace

Medical practitioners, psychologists and physical therapy providers often do not adequately identify and address 'flags' that can derail the effectiveness of standard clinical treatments including psychological therapies. These flags, such as potential psychosocial barriers including work problems, performance issues, conflict with the immediate manager and pre-existing psychological problems need to be identified early, communicated to rehabilitation providers and other relevant stakeholders and actively managed, to improve return to work outcomes.

### 5 Enable effective communication with treatment providers

Clinical service providers who assume an excessive advocacy role or have limited or ineffective communication with key stakeholders (e.g. employer representatives and insurers) achieve worse return to work outcomes.

For Workers' Compensation please contact Chris Jamieson on 02 9320 2751 or email Chris.Jamieson@echelonaustralia.com.au

For Group Salary Continuance please contact Stuart Whitbread on 02 9290 8023 or email Stuart.Whitbread@jlta.com.au

# A Reinsurer's Perspective...

In Australia, reinsurance plays a critical role for every licensed insurer with respects to portfolio / capital protection. In our previous edition of Building Blocks, comment was made from Chubb Insurance on the issue of risks exposed to natural catastrophe and made mention of the fact terms were changing across the insurance market as a whole. Reinsurance is essentially the mechanism where Insurance carriers protect their portfolio / balance sheet from extraordinary exposure which is usually attributable to natural catastrophes.

An Insurer licensed in Australia is required to have an effective framework for reinsurance management which includes a Reinsurance Management Strategy (REMS). This framework should have sound reinsurance management policies and procedures, clearly defined managerial responsibilities and controls and must be submitted annually to APRA.

The capital requirements for general insurance are also becoming more risk sensitive and there will be tighter limits on large investment exposures. Careful consideration will also be given to calculation of possible maximum loss (PML) and maximum event retention (MER) for the calculation of the minimum capital requirement (MCR) in terms of concentration of risk.

Over the course of 2011, Australia and New Zealand experienced an unprecedented level of natural catastrophe losses which have been compounded by extreme events in Japan and Thailand. According to preliminary estimates from Swiss Re's sigma team, total insured losses for the global insurance industry from natural catastrophes and man-made disasters reached USD 108 billion in 2011. This is more than double the figure of USD 48 billion in 2010. Claims from natural catastrophes alone reached USD 103 billion in 2011, compared to only USD 43 billion last year. The earthquake in Japan accounts for most of this year's economic losses. More than 30 000 people lost their lives due to catastrophes in the first eleven months of the year, most of them in Japan [source: Swiss Re Economic Research & Consulting Department].

JLT's Stuart Beatty believes that in 2012, insurers licensed In Australia will experience significant increases in reinsurance costs on their portfolio protections (circa 100%). They will also be re-assessing their views on various PML scenarios as the events that have happened in the region have exceeded previously held views on realistic disaster scenarios.

This will ultimately lead to insurers being more focussed on their accumulation of insurable interest in regions exposed to natural disasters - Australia and New Zealand are exposed extensively.

It will cost insurers more to protect their portfolios in the reinsurance capital markets with this increased cost being passed on by Insurers to policy holders. With respect to Real Estate schedules the principal exposure for an insurer will be the natural catastrophe exposure so it can be expected that increasing reinsurance costs will impact on real estate schedules in 2012. It is also likely that deductibles will increase and the breadth of coverage afforded will reduce as a result of these changing conditions.

In recognition of this market dynamic, JLT has established a market leading reinsurance entity in Australia that will be responsible for managing the reinsurance needs of insurance carriers in Australia and New Zealand.

Proactive focus on reinsurance terms will ultimately benefit the original client as our reinsurance team will be ensuring an insurance carrier's reinsurance needs are met in the most competitive manner available so capacity and premiums offered by insurance carriers are the best available considering all market dynamics.

JLT feels it is important to be able to control such marketing so that we deliver the best available capacity and pricing to our clients.

For more information contact Stuart Beatty on (02) 9290 8106 or email stuart_beatty@jltasia.com

## Health Check Alert

Does your policy have Conditions and Warranties?

Not complying with your policy Conditions and/or Warranties can have a significant impact on your ability to recover in the event of a loss.

## JLT Tip

**Ensure your broker has identified all of the Conditions and Warranties within your policy and that you understand their application.**

# Management of Unoccupied Properties

Vacant premises generally lead to increased frequency and severity of losses and this is why they require additional risk management. The Real Estate team at JLT has prepared this guide for property managers and landlords.

The increased exposure of vacant or void premises is less desirable to insurers who will look to amend their terms to reflect the perceived risk. Insurers may look to reflect the increased level of risks with the application of additional special terms, including increased excesses, increased premiums and/or restricting the cover.

The following precautionary actions are typical, and desired by insurers, for voids and/or unoccupied premises, but given the location and other specifics of each property some variations might apply on a case by case basis:

1 Regular inspections of the premises, including internally, should take place, preferably at least once a week, to ensure the property is fully secure and there are no signs of entry, damage, etc.

2 In the case of properties with 24 hour onsite security this internal inspection may be required less frequently, but the owner should ensure security staff are informed of the vacant areas and ask them to undertake regular external checks.

3 Water systems should be drained down or the heating set to maintain an ambient temperature of 5 degrees or above to prevent the pipes from freezing or bursting. Other services should be disconnected unless required to maintain temperature/detection systems, etc.

4 Valves should be chained and padlocked closed unless serving sprinkler or other critical systems, in which case they should be in the open position.

5 All existing physical security measures must be put into effect and ideally external doors to a property should be secured with five lever mortise deadlocks. However, depending on the type of doors, this may not be possible and if we can give further guidance in this regard we are happy to assist.

6 In some instances insurers may prefer external boarding of windows but if the building has 24 hour onsite security this might be waived, providing the external checks outlined above are being undertaken.

7 Any intruder and fire alarm detection systems must be set and maintained and any monitoring contracts continued in force.

8 Letter boxes should be securely blocked, ideally by screwing shut with non-return headed screws, so as to prevent any accelerants or lighted materials being passed through.

9 The empty property should be cleared of combustible waste both internally and externally. The regular checks should also look for signs of fly tipping, which can provide a would be arsonist with fuel for a fire and, if present, these should be removed as soon as possible.

10 Similarly, any damage or graffiti or overgrown vegetation which can indicate the vacant condition of premises should be repaired or removed as soon as possible.

11 Tanks containing heating fuel and other flammable products should be drained and precautions taken to prevent the explosion of residual vapours.

12 Where the site is open, the use of concrete blocks or ditches should be considered.

13 The maintenance of the property in a safe condition is also important. This is necessary to safeguard the health and safety of those performing the regular checks but also because the owner's / leaseholder's duty of care applies equally to trespassers, who might include children since empty space can attract them as a play area. This will almost certainly require a review of the formal health and safety risk assessments for the property.

14 Where voids are being maintained in condition for immediate letting and plant such as lifts and pressure systems are kept operational, owners need to ensure that they are inspected as required under the appropriate safety regulations. This needs particular awareness when such units are taken back from tenants who will previously have been responsible for such inspections and the property and its plant will need to be added to the owner's emergency inspection programme.

Ultimately all owners, tenants, managing agents and local property managers will have to use a degree of subjectivity as to what is most appropriate according to individual circumstances and in some cases legal advice might be necessary, but the JLT Real Estate team would be happy to provide advice if required.

For more information contact Stephen Cooper on (02) 9290 8123 or email Stephen.Cooper@jlta.com.au.

## Health Check Alert

Do you understand how your deductibles operate?

The proportion in which the insured retains themselves before insurance is triggered can be referred to by different names (for example Excess, Deductible and Retention). It is important to understand how your self insured retention operates before a loss is incurred.

## JLT Tip

**Read through your policy schedule and understand if a claim occurs whether there is an exact monetary amount that the insured retains or whether or not this is a percentage of the building sum insured. In Natural Catastrophe zones, the latter is becoming more common and with the percentages increasing the self insurance proportion can be significant.**

# Brownfields redevelopment – long term benefits and liabilities

Australia is one of the fastest growing advanced economies in the world at the moment with projections for nearly 3.3 million new households to be built by 2030 with the majority of these being built on "infill" or brownfield sites. [Source: National Housing Supply Council]

**XL Insurance's Environmental Underwriter, Andrew Hookings,** believes there are a variety of options available to mitigate these liabilities, but none is a cure for all. Environmental Impairment Liability (EIL) insurance can be a very effective tool in managing the risks of building on former industrial sites and can also provide long-term financial certainty to the parties involved.

Australia has a complex environmental legislation structure depending on which state you are operating in, but all are generally based on the "polluter pays" principle. As a result, buyers of brownfield land might think they have nothing to worry about as they are not the original polluter. However, changes in legislation as well as the way sale and purchase agreements are being drafted means the buyers can at times be left footing the cleanup bill.

Buyers are now undertaking rigorous due diligence assessments prior to purchasing the land. While this investigation for past pollution is now standard it should not necessarily be seen as a complete solution on its own. Pre-acquisition due diligence is typically done as a desk-based study of the site and its setting, like geology or sensitive watercourses nearby, historical usage and past pollution incidents. Where potential issues are identified a further detailed study including taking samples from the site would be carried out. But it will never offer a 100% guarantee.

Warranties and, increasingly, indemnities are also used to reduce the financial risk when buying former industrial land. However, indemnities, in particular, are only as good as the financial strength of the seller and may offer only limited protection. Environmental insurance provides a long-term comfort to the parties involved.

Another risk associated with developing a former industrial site to a more sensitive end use such as for residential purposes is the threat of third party claims or even changes in regulatory climate which may occur long after the site has been cleaned up and redeveloped. When cleaning a site some materials are frequently left in the ground as long as the contamination does not present an undue risk to human health and the environment. Though this might have been acceptable and within the law at the time of sale, there have been cases where the occupants of the site much later suffered bodily injury or property damage from the contamination.

One example is the case of a site which operated as a gasworks nearly a century ago and then was turned into residential homes. Years after the redevelopment toxic gases started to creep up from the ground causing illness to the new home owners and leading to an expensive cleanup operation.

Environmental laws are also constantly evolving and the regulator could, for instance, lower the thresholds deemed to be acceptable pollution. Alternatively, previously unknown contamination could be discovered leading to additional clean-up requirements. These potential issues can arise long after redevelopment and lead to extra costs years later.

As a result of the growing demand for this type of cover the insurance market has developed a flexible long-term environmental solution, usually for as much as 10 years. This insurance offers property developers control to manage their long-term risks while providing lenders a significant level of comfort when building homes on previously developed land.

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