How CRE Can Rise to the Challenge of Escalating Insurance Premiums

Catastrophic weather events are causing increased premiums and reduced coverage options, putting pressure on building owners and real estate managers to hone their property and risk management plans.

By Brian A. Lee

From recent Midwestern tornadoes to a 2024 hurricane season projected to produce 17 to 25 named storms, natural disasters are on the rise, spurring dramatic increases in commercial property insurance pricing. While some locations are more vulnerable than others, rising insurance rates are unavoidable. In the previous five years, commercial property insurance costs increased more than 70%, according to Moody's.

The cost to insure built assets in the last year has risen from 10 to 25%, reports Mike McConnell, CPM, an IREM instructor and property management consultant. One multifamily owner told the certified property manager to expect 20% rate increases when insuring new medium-sized apartment properties.

"It's pretty dramatic stuff, and the primary driving force is catastrophic events," McConnell says.

Losing Loss Control

When an insurer has to pay out more claims than planned, business losses ensue. As a result, coverage costs escalate for property owners.

That's why State Farm announced plans in March to non-renew about 72,000 policies in California, which followed its 2023 move to stop accepting new insurance applications for all business and personal property in the Golden State. Allstate, Farmers Insurance and The Hartford have since adjusted coverage in the state.

"It's a math problem: if they have more losses than their loss reserves can cover, then it's not good business, not an economically viable proposition for them," McConnell says. "In Florida, the state legislature has attempted to reduce insurers' risk exposure by modifying coverage regulations, but lawmakers can't legislate versus hurricanes and catastrophic loss, it's not possible."

What Property Owners & Managers Can Do

While an 'act of God' is obviously beyond human control, there are mitigation strategies property managers and owners can undertake to avoid or minimize potential weather risk. Planning is essential.

"A good risk management plan has always been a best practice in commercial real estate, and in today's environment it's absolutely required," McConnell says. "It all goes back to the Boy Scout motto of being prepared. You can't prevent disasters but you can have a plan to mitigate their impact."

A risk management plan must include identification and assessment, mitigation, monitoring and governance. For natural disasters, plans must cover both preparation and response. For non-weather-related risk, such as fire, it's important to have up-to-date alarms, extinguishers and sprinklers, and properly communicated and enforced rules and regulations (e.g., no grills on apartment balconies!).

Property managers should consult insurance advisors to improve the building components most impactful on rates. Roofs are huge factors for insurers in determining underwriting costs, McConnell asserts. Windows and security systems are also important.

McConnell recommends including on your risk management team an insurance broker and/or a risk advisor, whose knowledge of the insurance market will be critical for securing appropriate coverages at competitive rates. For example, they can advise on policy alternatives, such as parametric insurance, which eliminates the claims adjustment process, allowing money to reach policyholders quicker.

"One thing that might get overlooked is that when you go to buy or renew insurance, you need somebody on your side to market your business and comprehensive risk management plan," McConnell says. "A good loss record should be marketed to prospective insurers, while an owner with a bad loss record can show what they've done to overcome that and reduce their risk in the future."