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Hopitality  
Winter 2006



# "intouch"

With 2006 coming to an end, I thought it appropriate to use our year-end communique to review some of the "hot topics" that came up throughout the year in my client meetings.

I have received a number of questions as to the responsibility of insuring for tenant's improvements. This is the first topic I wanted to address as it not only affects everyone, but through understanding your responsibility, you may ultimately be able to lower your insurance costs.

Rates always top the "list of concerns", and while Lloyd Sadd deals with every Hospitality Insurer in the marketplace, I thought it might be a good idea to provide some light on the subject on how claims affect rates.

While we enjoy Alberta's booming economy, it brings up unique challenges that can impact your insurance. In the final section, I have identified some coverages that you might want to consider, and some existing coverages that definitely merit a review each year.

- 1) Tenant's Improvements – Who has the responsibility?
- 2) Claims and your Liability rates – The Explanation
- 3) Coverages for Consideration



## Tenant's Improvements – Who should insure them, landlord or tenant?

The short answer: Refer to your lease. In a recent review of several lease agreements, we noted several different arrangements between tenant and landlord. It is very important to understand your lease, to ensure that both landlord and tenant have adequate insurance (and in the tenant's case, perhaps they are over-insuring).

Most leases will make the landlord responsible for insuring any existing improvements when a new lease is signed, as they now are part of the building. If a tenant then decides to make improvements to their space, the lease will dictate who should be insuring the improvements, and for how long.

It is common for a lease (lets assume a 60 month lease) to say that the 1/60th of the improvements become the property of the landlord each month, with the landlord therefore owning all improvements upon the expiry of the lease. This being the case, the tenant should be insuring 100% of the tenant improvements in year 1, but each following year should consider insuring only the portion of the tenant's improvements for which they are responsible (this doesn't take into consideration rising construction costs which may offset the need to reduce limits). Likewise, the landlord should be increasing their insurance each year to account for the tenant improvements which now are considered part of the building. This is important, because the landlord may find themselves underinsured down the road if the lease dictates they are responsible for these tenant improvements. A landlord may find themselves facing co-insurance penalties, and incurring a substantial loss which they will be self-insuring.

Other leases may dictate that the improvements become the property of the landlord in 90 days. Again, the tenant should understand this so that they are not insuring tenant's improvements that really are not their responsibility (which could mean they are over-paying for insurance).

Certainly there are several other lease arrangements that could exist, so a review of your lease would be a great idea. I would be more than happy to review any lease documents and provide feedback from an insurance perspective. I would of course recommend that you consult your lawyer as well.



## Claims and Your Liability Rates - The Explanation

With hospitality Insurance, it typically isn't a matter of "if" there will be a claim...It's usually thought of as a matter of "when"...The most well-run, risk-conscious bar in the world will still likely face a claim at some point...our increasingly litigious society, lawyers taking on cases for contingency making it "affordable to sue", precedents set by the courts over the years...the list of reasons runs long.

The issue of "joint and several liability" makes things worse for bars...i.e. A situation where you serve a patron his first drink, and he consumes 20 more elsewhere. A court can find you 5% at fault for an ensuing "incident", but you can end up being on the hook for 100% of the claim under certain circumstances. Exposures such as slip-and-falls, patron on patron violence etc, allegations that staff forcibly evicted a patron... These scenarios all have the potential for large lawsuits, and are impossible for any bar-owner to prevent entirely...insurers still have to defend even fraudulent allegations.

One of the key issues, and one of the main difficulties Insurers have with hospitality risks, is the long "tail"... i.e. they can go a year or two thinking they are profiting, but claimants have 2 years to file a statement of claim, and then additional time to serve the claim. As the policies are "occurrence based", the claim is assessed to the Insurer who was on risk on the date the incident occurred. In the past, this has been the downfall of many Insurers who got involved in Hospitality. Years after they recognized they weren't profitable and stopped writing hospitality accounts, they were still paying millions of dollars in claims on what they had written.

Insurers are conscious as to the problems other Insurers have faced in years past. For that reason, Insurers don't jump to discount rates each year because they think they have turned a profit...it will be several years before they know their true results for any given year. This is something that is somewhat unique to hospitality Insurance. They always have to consider claims that are "incurred but not yet reported (IBNRs)"

On the positive side, Insurers prepare for claims...they expect them to happen. Therefore, when you do have a claim, Insurers don't automatically triple rates, or like in years past, get off risk entirely. The important things are to (a) show that you have written procedures/training etc making these claims less likely to occur, and (b) you take steps after the claim so that the same incident won't occur the next time.

Actuaries do an ongoing study of claims data, and advise Insurers where rates need to in order to pay claims and hopefully make a profit (they are a business). Clients that show they take those extra steps (and show a positive claims history) will usually get credits, while those having claims problems will often see some surcharges or perhaps deductible increases. As a broker, it is my job to ensure that every year, we highlight all those things that make your business "best in class" and ensure that you are always on the low-end of the rate spectrum.

I would be more than happy to answer any questions you might have on this topic.

On a sidenote, you may want to consider a review of your liability limits. During the "hard market", many owners reduced their liability limits to off-set the huge premium increases. Each year however, Insurers tell us that they are seeing more "large losses", and that the average settlement/judgement has also gone up (this likely won't change). As premiums have come down to at least a more reasonable level, consideration should be given as to your liability limits to protect your company.

In the last year or two, there have been a number of insurance settlements in Canada ranging from \$2,000,000 to a high of \$12,000,000.

## Coverages for Consideration

Almost every week, I see a claim or two come across my desk. As a broker specializing in Hospitality, I see it my role to have a thorough understanding of your business, and be aware of the exposures that can affect your business. My role is to work with you in identifying exposures you may have, and work with you in deciding which ones you want to insure against, and others that you may simply want to self-insure. Certain coverages may have been declined in the past, and now may want to be reconsidered. In other cases, we are identifying new coverage available, which may be applicable to your business.

### Employee Dishonesty

Provides coverage for the loss of money and securities and other property used in your business due to dishonesty or fraud by any of your employees. The limit shown is the maximum amount payable, regardless of the number of employees involved in the loss, and includes a "discovery period" of one year. \$10,000 limit is approximately \$350 annually. Most bar owners carry crime coverage but excluding Employee Dishonesty. In the past, many Insurers didn't want to offer Employee Dishonesty...this is no longer the case.

### Extra Expense

This coverage is usually purchased in addition to standard "business interruption coverage". This provides funds to meet added expenses necessary to maintain the normal conduct of your business after a loss by an insured peril (consider a partial loss where you can potentially re-open for the upcoming weekend). This includes such expenses as rental of temporary equipment, special advertising, extra and overtime help. \$10,000 limit is approximately \$250 annually.

### Consequential Loss including Off Premises Power

Covers loss or damage to contents (consider stock that might have to be thrown out) due to change of temperature when caused by an insured peril. This includes damage to refrigeration or cooling apparatus as well as off premises public utility plants, transformers, etc that provide electrical heat, light or power to the premises.

### Damage to Building by theft

Refer to lease agreement. In many leases, the tenant is made responsible for any damage to the building that occurs during a theft. Some Insurers include a small sublimit in their policies, but often a higher limit should be considered. Premium for \$10,000 is approximately \$150-200. On a related note, it is a good idea to review your lease as to responsibility for covering plate glass.

On the same topic, I thought I would also include a couple "coverage reminders"....

### Crime Coverage

Coverage is limited overnight, or when the business is closed, to \$250 unless money is being stored in a minimum Class 2 safe (ATM's and VLT's are not Class 2 safes).

### Property Insurance

Construction rates have been climbing steadily for the last 3 years. Please review your limits to ensure that they remain adequate for "replacement cost" (i.e. new). The limits on your policy are the maximum an Insurer will pay for a loss, and in the event of a partial loss, you will be penalized by the Insurer if you are underinsured. Basically, if you are insuring at a limit which is half the cost to replace, you will only receive half of your loss.

### Business Interruption

While every client carries Business Interruption, I would strongly recommend the completion a "profits worksheet" that will ensure your limit is sufficient. Business Interruption is intended to cover your loss in profits, plus all standing charges during the shut-down (i.e. those expenses that continue during a loss). It is a one-page sheet, and is very helpful to have on-hand in the event of a loss (to help "prove your loss"). On another note coverage under your "standard policy" is up to a maximum of 12 months. Consideration should be given as to how long you may actually be out of business (i.e. how long would it take in today's market to rebuilding the building, and then re-build your bar). Indemnity periods can be extended to 18 months or 24 months if required.

If you have any questions about your current insurance program, please call me anytime, or alternatively, you can reach my Account Manager, Andrew Duncan at 930-3811. We would be more than happy to obtain quotes for any additional coverage from your Insurer.

Often, it isn't until a claim occurs that one questions the adequacy of their coverage. We are always happy to discuss any insurance concerns you might have, and work with you to ensure that we have coverage in place that looks after any exposures you might have.

I would appreciate any feedback as to the content of our communiques, and would be more than happy to answer any questions or discuss the topics further. If there are topics you would like us to address, please call me anytime.

I wish everyone the best over the holidays, and look forward to working with you in the new year.

Sincerely

Luke Horcica



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